APPENDIX A

Statute Involved

RATES AND CHARGES; SCHEDULES; SUSPENSION OF NEW RATES

SEC. 4. (a) All rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) No natural-gas company shall, with respect to any transportation or sale of natural gas subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from the date this act takes effect) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regu-

lations, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, State Commission, or gas distributing company[18] or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect;[18] and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period, on

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[18] Subsection 4 (e) was amended May 21, 1962 by Public Law 87-454, 87th Congress, 2d Session [S. 1595], 76 Stat. 72.

motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective, the Commission may, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible. [52 Stat. 822 (1938); 76 Stat. 72 (1962); 15 U.S.C. § 717c]

FIXING RATE AND CHARGES; DETERMINATION OF COST OF PRODUCTION OR TRANSPORTATION

SEC. 5. (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however*, That the Com-

mission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural-gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural-gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

(b) The Commission upon its own motion, or upon the request of any State commission, whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transportation of natural gas by a natural-gas company in cases where the Commission has no authority to establish a rate governing the transportation or sale of such natural gas. [52 Stat. 823 (1938); 15 U.S.C. § 717d]

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EXTENSION OF FACILITIES; ABANDONMENT OF SERVICE

SEC. 7. (a) Whenever the Commission, after notice and opportunity for hearing, finds such action necessary or desirable in the public interest, it may by order direct a natural-gas company to extend or improve its transportation facilities, to establish physical connection of its transportation facilities with the facilities of, and sell natural gas to, any person or municipality engaged or legally authorized to engage in the local distribution of natural or artificial gas to the public, and for such purpose to extend its transportation facilities to communities immediately adjacent to such facilities or to territory served by such natural-gas company; if the Commission finds that no undue burden will be placed upon such natural-gas company thereby: *Provided*, That the Commission shall have no authority to compel the enlargement of transportation facilities for such purposes, or to compel such natural-gas company to establish physical connection or sell natural

gas when to do so would impair its ability to render adequate service to its customers. [52 Stat. 824 (1938); 15 U. S. C. § 717f (a)]

(b) No natural-gas company shall abandon all or any portion of its facilities subject to the jurisdiction of the Commission, or any service rendered by means of such facilities, without the permission and approval of the Commission first had and obtained, after due hearing, and a finding by the Commission that the available supply of natural gas is depleted to the extent that the continuance of service is unwarranted, or that the present or future public convenience or necessity permit such abandonment. [52 Stat. 824 (1938); 15 U. S. C. § 717f (b)]

(c) [2] No natural-gas company or person which will be a natural-gas company upon completion of any proposed construction or extension shall engage in the transportation or sale of natural gas, subject to the jurisdiction of the Commission, or undertake the construction or extension of any facilities therefor, or acquire or operate any such facilities or extensions thereof, unless there is in force with respect to such natural-gas company a certificate of public convenience and necessity issued by the Commission authorizing such acts or operations: *Provided, however*, That if any such natural-gas company or predecessor in interest was bona fide engaged in transportation or sale of natural gas, subject to the jurisdiction of the Commission, on the effective date of this amendatory Act, over the route or routes or within the area for which application is made and has so operated since that time, the Commission shall issue such certificate without requiring further proof that public convenience and necessity will be served by such operation, and without further proceedings,

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[2] Subsection 7 (c) amended; (d), (e), (f) and (g) added February 7, 1942 by Public Law No. 444, 77th Congress, Chapter 49, 2d Session [H.R. 5249], 56 Stat. 83, 84.

if application for such certificate is made to the Commission within ninety days after the effective date of this amendatory Act. Pending the determination of any such application, the continuance of such operation shall be lawful.

In all other cases the Commission shall set the matter for hearing and shall give such reasonable notice of the hearing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by the Commission; and the application shall be decided in accordance with the procedure provided in subsection (e) of this section and such certificate shall be issued or denied accordingly: *Provided, however*, That the Commission may issue a temporary certificate in cases of emergency, to assure maintenance of adequate service or to serve particular customers, without notice or hearing, pending the determination of an application for a certificate, and may by regulation exempt from the requirements of this section temporary acts or operations for which the issuance of a certificate will not be required in the public interest. [52 Stat. 825 (1938), as amended, 56 Stat. 83 (1942); 15 U. S. C. § 717f (c)][3]

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[3] As originally enacted June 21, 1938 by Public Law No. 688, 75th Congress, Chapter 556, 3d Session [H.R. 6586], 52 Stat. 825, Section 7 (c) read as follows:

"(c). No natural-gas company shall undertake the construction or extension of any facilities for the transportation of natural gas to a market in which natural gas is already being served by another natural-gas company, or acquire or operate any such facilities or extensions thereof, or engage in transportation by means of any new or additional facilities, or sell natural gas in any such market, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require such new construction or operation of any such facilities or extensions thereof: *Provided, however*, That a natural-gas company already serving a market may enlarge or extend its facilities for the purpose of supplying

(d) [4] Application for certificates shall be made in writing to the Commission, be verified under oath, and shall be in such form, contain such information, and notice thereof shall be served upon such interested parties and in such manner as the Commission shall, by regulation, require. [56 Stat. 84 (1942); 15 U. S. C. § 717f (d)]

(e) [5] Except in the cases governed by the provisos contained in subsection (c) of this section, a certificate shall be issued to any qualified applicant therefor, authorizing the whole or any part of the operation, sale, service, construction, extension, or acquisition covered by the application, if it is found that the applicant is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Act and the requirements, rules, and regulations of the Commission thereunder, and that the proposed service, sale, opera-

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increased market demands in the territory in which it operates. Whenever any natural-gas company shall make application for a certificate of convenience and necessity under the provisions of this subsection, the Commission shall set the matter for hearing and shall give such reasonable notice of the hearing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by the Commission. In passing on applications for certificates of convenience and necessity, the Commission shall give due consideration to the applicant's ability to render and maintain adequate service at rates lower than those prevailing in the territory to be served, it being the intention of Congress that natural gas shall be sold in interstate commerce for resale for ultimate public consumption for domestic, commercial, industrial, or any other use at the lowest possible reasonable rate consistent with the maintenance of adequate service in the public interest." (52 Stat. 825 (1938))

Public Law No. 444, 77th Congress, Chapter 49, 2d Session [H.R. 5249], 56 Stat. 83, which amended Section 7 (e), effective February 7, 1942, was enacted after the Commission's decision *In the Matter of Kansas Pipe Line & Gas Company*, 2 F.P.C. 29.

[4], [5], [6] See footnote 2, p. 7.

tion, construction, extension, or acquisition, to the extent authorized by the certificate, is or will be required by the present or future public convenience and necessity; otherwise such application shall be denied. The Commission shall have the power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require. [56 Stat. 84 (1942); 15 U. S. C. § 717f (e)]

(f) [6] The Commission, after a hearing had upon its own motion or upon application, may determine the service area to which each authorization under this section is to be limited. Within such service area as determined by the Commission a natural-gas company may enlarge or extend its facilities for the purpose of supplying increased market demands in such service area without further authorization. [56 Stat. 84 (1942); 15 U. S. C. § 717f (f)]

(g) [7] Nothing contained in this section shall be construed as a limitation upon the power of the Commission to grant certificates of public convenience and necessity for service of an area already being served by another natural-gas company. [56 Stat. 84 (1942); 15 U. S. C. § 717f (g)]

(h) [8] When any holder of a certificate of public convenience and necessity cannot acquire by contract, or is unable to agree with the owner of property to the compensation to be paid for, the necessary right-of-way to construct, operate, and maintain a pipe line or pipe lines for the transportation of natural gas, and the necessary

[7] See footnote 2, p. 7.

[8] Subsection 7 (h) was added July 25, 1947 by Public Law No. 245, 80th Congress, Chapter 333, 1st Session [H.R. 2956], 61 Stat. 459.

land or other property, in addition to right-of-way, for the location of compressor stations, pressure apparatus, or other stations or equipment necessary to the proper operation of such pipe line or pipe lines, it may acquire the same by the exercise of the right of eminent domain in the district court of the United States for the district in which such property may be located, or in the State courts. The practice and procedure in any action or proceeding for that purpose in the district court of the United States shall conform as nearly as may be with the practice and procedure in similar action or proceeding in the courts of the State where the property is situated: *Provided*, That the United States district courts shall only have jurisdiction of cases when the amount claimed by the owner of the property to be condemned exceeds $3,000. [61 Stat. 459 (1947); 15 U. S. C. § 717f (h)]

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APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 17582

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT
CONTINENTAL OIL COMPANY AND SUNRAY D X OIL COMPANY, SKELLY OIL COMPANY, SUN OIL COMPANY, GEORGE H. COATES, PRADO OIL & GAS COMPANY, PHILADELPHIA ELECTRIC COMPANY, INTERVENORS

No. 17627

CONTINENTAL OIL COMPANY AND SUNRAY D X OIL COMPANY, PETITIONERS

v.

FEDERAL POWER COMMISSION, RESPONDENT
PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, THE UNITED GAS IMPROVEMENT COMPANY, AND LONG ISLAND LIGHTING COMPANY, INTERVENORS

No. 17628

THE UNITED GAS IMPROVEMENT COMPANY, AND LONG ISLAND LIGHTING COMPANY, PETITIONERS

v.

FEDERAL POWER COMMISSION, RESPONDENT
SUN OIL COMPANY, SOUTH TEXAS NATURAL GAS GATHERING COMPANY, GEORGE H. COATES, SKELLY OIL COMPANY, CONTINENTAL OIL COMPANY, et al., PRADO OIL AND GAS COMPANY, AND PHILADELPHIA ELECTRIC COMPANY, INTERVENORS

No. 17859

PRADO OIL AND GAS COMPANY, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT
PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, INTERVENOR

On Petitions to Review Orders of the Federal Power Commission

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Decided January 23, 1964

Opinion

Before FAHY, WASHINGTON and DANAHER, *Circuit Judges*.

FAHY, *Circuit Judge*: Continental Oil Co. and Sunray D X Oil Co., petitioners in No. 17627, and Prado Oil and Gas Co., petitioner in No. 17859, on May 15, 1959, and June 30, 1960, respectively, entered into contracts with the South Texas Natural Gas Gathering Company for the sale of natural gas at a price of 16 cents per Mcf. This was part of a larger project involving sales by numerous other gas producers in Texas Railroad District No. 4 to South Texas, to be delivered to Transcontinental Gas Pipe Line Corporation, for resale to interstate commerce. Applications for approval by the Federal Power Commission of sales of the petitioning producers were first filed between May 1959 and January 1960. However, even before notice of these applications had been issued *ex parte* temporary certificates had been granted to most of the producer-applicants authorizing the immediate commencement of the sales at contract prices ranging from 9 to 17 cents per Mcf. None of these certificates provided for any re-

fund should the contract prices subsequently be found to exceed the proper "in-line" price for the area.

After a hearing on the applications the Commission on November 22, 1960, approved the producers' proposed prices. The Public Service Commission of the State of New York, petitioner in No. 17582, sought a rehearing, contending that the proper "in-line" price for the particular area was 14.6 cents per Mcf. The Commission granted a rehearing and consolidated the above applications with thirty-five additional producer applications relating to the same project. Like the producers involved in the first stage of the proceedings these additional producer-applicants had been granted temporary operating certificates containing no refund provision. Hearings were once again held and on January 25, 1962, the Presiding Examiner issued his preliminary statement approving the proposed sales at prices ranging from 16 to 17 cents. In doing so he relied heavily on the Commission's Statement of General Policy No. 61-1, issued September 28, 1960, in which, as a part of its area pricing policy, the Commission had set the area price for Texas Railroad District No. 4, the origin of the gas, at 18 cents per Mcf.

On August 30, 1962, the Commission issued its own final decision in which it found that the "in-line" price for the area with respect to contracts entered into prior to September 28, 1960, was 15 cents per Mcf.[1] Accordingly, it approved the sales in question on the condition that the

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[1] Of eighty-six related applications originally involved in the Commission proceedings only fifteen proposed contract prices were found to be "out of line"; and of the twelve producers whose certificates were conditioned by the Commission on a price reduction all but three, Continental, Sunray and Prado, have apparently accepted the Commission's ruling by not filing a petition for review.

price charged be not in excess of 15 cents.[2] It refused, however, to order a refund of the charges in excess of 15 cents collected under the temporary authorizations. The Commission was initially of the opinion that since no refund provision had been included in the temporary certificates there was "no basis for ordering refunds." In its later order of December 18, 1962, denying reconsideration, the Commission explained that it would be inequitable to require refunds when the temporary certificates contained no provision clearly apprising the producers of the risk in operating under a temporary certificate subject to a refund obligation.

In its final orders the Commission also declared that the provisions in the sales contracts obligating the purchaser to take or pay for a minimum volume of gas on an annual basis were subject to the Commission's final order in a pending rule making proceeding concerning "take or pay" provisions. The Commission subsequently modified this condition so that the producers would not be required to file "take or pay" provisions for less than eight per cent of the annual contract quantities, regardless of the outcome of the rule making proceeding.

The producer petitioners in Nos. 17627 and 17859 seek review of the orders insofar as they condition approval of the proposed sales (a) on a reduction in the initial price to 15 cents and (b) on the outcome of the rule making proceedings regarding "take or pay" provisions. Petitioners in Nos. 17582 and 17628 seek review of the same orders insofar as they omit to require a refund of excess charges collected under the temporary certificates. Inter-

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[2] Simultaneously with this order the Commission issued its Fifth Amendment to Statement of General Policy No. 61-1 in which it reduced the area ceiling price level for Texas Railroad District No. 4 from 18 cents per Mcf. to 16 cents per Mcf.

venors in Nos. 17582 and 17628 support the Commission in refusing to order refunds.[3]

The Fixing of An In-Line Price of 15 Cents as a Condition to the Permanent Certificates

The Commission was obliged to be guided by *Atlantic Ref. Co.* v. *Public Serv. Comm'n.* 360 U.S. 378 (1959), known as the *Catco* decision. The Court there pointed out that some of the provisions of the Act regarding rates, notably Sections 4 and 5, entail extremely long delays, calling upon the Commission in Section 7 proceedings to condition certificates by requiring an "in-line" initial price. Accordingly, in granting permanent certificates the Commission is to decide the "in-line" price. This the Commission did in the present cases, fixing it as of the date of the contracts under which the gas was to enter interstate commerce. It determined that the appropriate price for District No. 4 revolved around the situation prevailing there in the years 1958, 1959 and 1960. It considered as the most important evidence a study prepared by the Commission staff analyzing contract and price data for the years 1955 and later. Of the contracts thus analyzed none executed during the 1958 to 1960 period and under permanent certificates involved prices above 18 cents and the majority, involving also the greater volume of gas, were at prices between 14 and 15 cents. And the Commission

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[3] In No. 17628 intervenor The South Texas Natural Gas Gathering Company refers to a statement in the brief of petitioners in that case regarding the absence of a provision in its certificate for a "flow-through" of refunds. South Texas states it would agree voluntarily to pass along refunds should they result from this review proceeding, on the condition that petitioners and other customers of Transcontinental Gas Pipe Line Corporation agree that such refunds will be immediately and completely passed along by them to the ultimate consumers so that petitioners and other customers of Transcontinental would not receive a windfall as the result of South Texas' action.

noted that it had granted certificates for sales in the area during the three years mentioned at prices ranging down to 6 cents per Mcf.[4] In addition, as the opinion points out, nearly all the contracts with prices above 15 cents were subject to litigation. Being under a cloud they were eliminated from consideration. The Commission also placed under the same cloud, or in a suspect category, other contract prices above 15 cents which, though not themselves in litigation, appeared because of the higher prices to be subject to the same infirmities as those which were. The Commission also gave less consideration to prices allowed under temporary certificates than under permanent certificates, because the former were issued ex parte and informally, without full investigation.

It cannot be seriously contended that the data upon which the Commission relied fails to support its determination of an "in-line" price of 15 cents. It is principally urged that the Commission erred in limiting, as above indicated, the evidence upon which it relied. We now consider these limitations.

As to the exclusion of prices under a cloud the Commission has the support of the opinions of the courts in *United Gas Improvement Co.* v. *FPC*, 283 F.2d 817, 824 (9th Cir. 1960), *cert. denied sub nom. Superior Oil Co.* v. *United Gas Improvement Co.*, 365 U.S. 879, and *California Co.* v. *United Gas Improvement Co.*, 365 U.S. 881 (1961), and *United Gas Improvement Co.* v. *FPC*, 290 F.2d 133, 137 (5th Cir.), *cert. denied sub nom. Sun Oil Co.* v. *United*

[4] Continental contends this finds no support in the record. In its opinion on reconsideration the Commission adequately meets this objection by pointing out that the notice it took of prices ranging down to 6 cents "was not a part of the decisional process in determining the line but merely part of our explanation of the scope of the staff exhibit, which treated sales at prices of 14 cents and above. Therefore further evidence on this matter would not affect the basis of our decision."

Gas Improvement Co., 368 U.S. 823 (1961), and see our opinion in *Pub. Serv. Comm'n* v. *FPC*, 109 U.S. App. D.C. 292, 295 n. 3, 287 F.2d 146, 149 n 3 (1960), *cert. denied sub nom. Hope Natural Gas Co.* v. *Pub. Serv. Comm'n*, 365 U.S. 880, and *Shell Oil Co.* v. *Pub. Serv. Comm'n*, 365 U.S. 882 (1961). In the light of these authorities we do not sustain the challenge advanced on this ground. In any event the exclusion of the prices under a cloud does not undermine the validity of the "in-line" price determined by the Commission, considering the evidence in its entirety.

The producer-petitioners make special objection to the Commission's refusal to rely upon a number of sales at 16 to 17 cents made in 1955 and 1956 to the Coastal Transmission Corp. Since the Coastal sales were made before the 1958-to 1960 period when the contracts in the present cases were entered into and since the majority of the subsequent sales in Texas Railroad District No. 4 were at less than 15 cents, the Commission could reasonably determine as it did that the Coastal sales did not establish a valid line of 16 to 17 cents for that area during the 1958 to 1960 period.

The Commission also pointed out that "the earlier Coastal sales were made to a new company that had neither been given a certificate nor was yet in operation, so may have resulted in higher prices than would have resulted from contracts with an established pipeline." The Commission substantiated this observation on appeal by pointing out that the staff exhibit showed for the 1955-1956 period when the earlier Coastal sales were made that other sales, involving a greater volume of gas, were made to a more established pipeline at prices below 15 cents.

Continental contends that the Commission erred in not considering certain costs and financial requirements, evidence with respect to which was presented to show the amount Continental would be required to receive to recoup

its cash outlay with respect to one area of its production here involved, and in failing to consider evidence as to the industry's replacement costs of gas, submitted by Texaco[5] and adopted by the other producers. However, these are not rate cases of the type in which evidence of this kind ordinarily is considered relevant. These proceedings under Section 7, considered with the *Catco* decision, permit the Commission to fix the "in-line" price, not on a basis of cash outlay or replacement costs, but on the basis of the price level established by comparable sales contracted for by those placing gas in the area in interstate commerce. The standards of Sections 4 and 5 are not those to be used in conditioning a certificate issued under Section 7; otherwise the purpose of *Catco* to avoid the consequences of the well nigh interminable proceedings incident to a rate case would be defeated. See, for example, *United Gas Improvement Co.* v. *FPC*, *supra*, 283 F.2d at 828. Consideration of the proffered evidence was not essential. In so deciding we need not hold that the Commission may never consider such evidence if the circumstances in a particular case move it to do so consistently with its obligations under *Catco*.

Prado contends in No. 17859 that the Commission failed to give adequate consideration to its own Statement of General Policy No. 61-1, as amended, issued September 28, 1960. By this Statement the Commission prescribed guide line initial prices for twenty-three producing areas. It said that in doing so it considered many factors, including cost information from all decided and pending cases, existing and historical price structures, volumes of production, trends in production, et cetera. The guide line initial price for Texas Railroad District No. 4 was 18 cents per Mcf. Thereafter, on August 30, 1962, concurrently with its opinion in No. 362, presently before us,

[5] The contention in this regard is made by Prado as well as Continental.

the area initial price for said District was lowered to 16 cents per Mcf. Prado contends that the action of the Commission in conditioning the permanent certificates at a price level below either the 18 cents or 16 cents guide line price is arbitrary and discriminatory. But the area guide line price is only a guide line price; it is not an "in-line" price required by *Catco* to be determined with the issuance of permanent certificates under Section 7(c). As the Commission states, its Policy Statement was a guide to its future action and "cannot effect an automatic approval of proposed rates, particularly where the contracts were entered into before the Policy Statement." The Commission could not have ignored altogether its own Policy Statement, but was not required to be controlled thereby in deciding, in the Section 7 proceedings, that the in-line price should be fixed at a less amount on the basis of the evidence analyzed in its opinion.

A somewhat related contention is that the Commission erred in fixing the "in-line" price as of the date of the contracts rather than as of the later date of initial delivery of gas. The Commission answers that the execution of a contract is the significant act of a buyer and seller in determining price, and that the effect of this determination does not await deliveries. We think we must honor the discretion thus exercised by the Commission "to require that the gas be sold under contracts that were in-line as of the time they were executed," to adopt its language. The Commission cites *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332 (1956), to the effect that rates are established initially by the companies by contract or otherwise. The Commission apparently made no general rule for all cases, for it states that "under the circumstances here" the contract prices must be in line as of the time the contracts were executed.

None of the attacks on the "in-line" determination gives the court a basis for holding it to be invalid; and since

the data relied upon adequately supports the price condition of the permanent certificates such condition is approved. Contracts under permanent certificates at prices of not more than 15 cents, covering such a large volume of gas from the same area, and for the years which are most relevant, are so numerous that we cannot say that the Commission exceeded its authority in fixing the "in-line" price at 15 cents, notwithstanding its refusal to give significant consideration to higher prices for earlier years, even though under permanent certificates.

The Take-Or-Pay Provision

The original condition in this regard reads:

> The certificates of all of the producer applicants . . . shall be conditioned so that the take-or-pay requirement in each contract is subject to the provisions of our final order in Docket No. R-199 as of the effective date of that order.

As we have said, in its decision on reconsideration the Commission modified this provision to read that "the producers shall not be required to file take-or-pay provisions for less than 80 per cent of the annual contract quantities."

Docket No. R-199 is the general rule-making proceeding to consider standardization of take-or-pay provisions in producer contracts. Any modification of such contracts which might be required as a result of the proceeding would be prospective only. Should the producers here involved be required to file modified provisions they could then obtain review. See *Midwestern Gas Transmission Co.* v. *FPC*, 292 F.2d 119 (5th Cir. 1961). The present impact of the proceeding in Docket No. R-199 is too tenuous and uncertain to require the court to pass now upon the validity of what might eventuate, or to hold invalid pursuit of the matter by the Commission. To do

the latter would be to say that no modification of the questioned provisions can be validly accomplished. And to do this now would be to rule in the dark.[6]

The Refund Issue

Petitioners, Public Service Commission of New York, United Gas Improvement Company and Long Island Lighting Company, intervenors before the Commission, contend in Nos. 17582 and 17628 that the Commission is under legal obligation to require as a condition to its grant of permanent certificates that the producers refund that portion of the charges they have collected under temporary certificates in excess of the maximum initial price found by the Commission to be required by the public convenience and necessity.

We consider first the producers' contention that the issuance of the temporary certificates were appealable orders and that the failure of petitioners in Nos. 17582 and 17628 to seek review thereof precludes the relief they now seek, citing *Texaco, Inc.* v. *FPC*, 290 F.2d 149, 156-57 (5th Cir. 1961). But there the challenged conditions were in the temporary certificates. The Court held that if those conditions were deemed to be invalid the question should have been raised before the challenging producers accepted the certificates. "This is true because the failure of petitioners to appeal from the order granting the conditions within the time provided for appeals in Section 19(b) of the Natural Gas Act . . . deprives this court of jurisdiction to entertain a petition to review this order. Clearly, the

[6] Petitioners in No. 17627 attack the validity of the Commission's Fifth Amendment to its Statement of General Policy No. 61-1. However, in determining the validity of the orders under review we need not probe the validity of the Amendment; and there is no occasion now to pass upon the Amendment independently of those orders.

order granting the temporary certificates, when it embodied the conditions now complained of was an order which then aggrieved the petitioners." *Id.* at 156-57.

The situation here is significantly different. It is true the present petitioners in a loose sense may be said to have been aggrieved by the absence of a refund condition in the temporary certificates, for such a condition would have strengthened their position; but in a jurisdictional sense their aggrievement is with the absence of a refund requirement in the permanent certificates over which we now have jurisdiction. Once this absence became final before the Commission timely review was sought. In this situation we think it is open to petitioners to obtain now a decision on the refund issue.

Coming to the merits the producer intervenors say a refund condition is beyond the Commission's statutory power. As to this we may say initially that our statement in *Atlantic Ref. Co.* v. *FPC*, —— U.S. App. D.C. ——, 316 F.2d 677, 679 (1963), that there is no mechanism for refund of overcharges under Section 7 is not a holding that a refund may never be required when a permanent certificate takes over from a temporary one, an issue not there considered.

The producers argue that in any event refunds may not be required because the Commission lacks power "to set retroactive rates or award reparations," citing *Hope Natural Gas Co.* v. *FPC*, 134 F.2d 287, 309-10 (4th Cir. 1943), *rev'd on other grounds*, 320 U.S. 591 (1944). But there the Court was referring to the power of the Commission with respect to rates which had become unconditionally effective when filed, subject to being changed only prospectively in a proceeding under Sections 4 or 5(a) of the Act. The Court was not ruling upon the power of the Commission to condition a permanent certificate by requiring refunds of excessive prices charged and received

under temporary certificates.[7] We think it is clear that a refund can be required when the temporary certificate is so conditioned. The serious question is whether it can be required when the temporary certificate is not so conditioned.

As to this the Commission itself, though it did not require refunds in these cases, does not disclaim the power. The basic purpose of the Natural Gas Act is consumer protection from unreasonable prices, and refund of excessive utility rates is a well recognized remedy. It would need to be quite clear from the Act that the Commission lacked the power to use such a remedy for the courts to deny it. We find no such clarity. The power does not depend upon an explicit refund provision in a temporary certificate. Should the occasion be appropriate for its exercise the power resides in the Commission when it grants a permanent certificate. To hold that it may not then require refund of excessive prices previously permitted without notice or hearing or mature consideration, since the Commission acted on an emergent and temporary basis, would be inconsistent with the regulatory responsibility of the Commission to aid in the ascertainment and authorization of just and reasonable rates.

Section 7(e) provides, "The Commission shall have the power to attach to the issuance of the certificate . . . such reasonable terms and conditions as the public convenience and necessity may require." 56 Stat. 84 (1942), 15 U.S.C. § 717(f)(e) (1958). And the temporary certificates before us provide:

> This acceptance for filing shall not be construed as constituting approval of any rate, charge, classifi-

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[7] As to the power see *Texaco, Inc.* v. *FPC*, 290 F.2d 149, 156 (5th Cir. 1961); *Pure Oil Co.* v. *FPC*, 292 F.2d 350, 352-54 (7th Cir. 1961). Compare, however, *Sunray Mid-Continent Oil Co.* v. *FPC*, 270 F.2d 404 (10th Cir. 1959).

cation, or any rule, regulation or practice affecting such rate or service contained in the rate filing; nor shall such acceptance be deemed as recognition of any claimed contractual right or obligation associated therewith; and such acceptance is without prejudice to any findings or orders which may be made in the final disposition of this proceeding or any other findings or orders which have been or may hereafter be made by the Commission in any proceeding now pending or hereafter instituted by or against your company.

* * * * * * *

This constitutes all requisite temporary authorization to commence the sale of gas, but such authorization and acceptance of the rate schedule are without prejudice to such final disposition of the certificate application as the record may require and, furthermore, once service is commenced under this authorization it may not be discontinued without permission of the Commission issued pursuant to the provisions of the Natural Gas Act.

These provisions, all else aside, amply support authority for conditioning the permanent certificates by a refund requirement. As we have indicated, to order refund of rates found to be excessive is not an unusual remedy; and it is not unavailable under the Natural Gas Act due to the fact that in some instances the parties are not explicitly notified early in the proceedings that such a remedy may be imposed.[8]

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[8] The producers rely upon the Tenth Circuit's decision in *Sunray Mid-Continent Oil Co.* v. *FPC*, 270 F.2d 404 (1959). The Court there held that even in attaching a refund condition to a temporary certificate the Commission must limit it by setting a price at or below which the producer can sell without risk of a subsequent

The existence of the power, however, does not mean that its exercise is mandatory, as petitioners in Nos. 17582 and 17628 assert. Here we follow the standard adopted by the Commission, namely, the standard of equity—that is, the issue of a refund in the present circumstances turns upon equitable considerations. But we do not follow the Commission in holding also that the sole and decisive equitable consideration here is the absence of a refund requirement in the temporary certificates. That would amount to saying that in the absence of such a condition in the temporary certificates refunds may not be required, a position we cannot accept. We recognize the Commission's duty to consider the extent to which a refund obligation in the absence of prior warning will, by increasing the risk producers must bear, affect the quantity and continuity of the supply of gas and thus have an adverse effect on the interests of consumers. But there are public interest factors of equity which must be weighed along with the effect of mere absence of a refund condition in the temporary certificates. One of these is the very fact that excessive prices were obtained while the proceedings pended, and after it wa sknown an "in-line" price above 14.6 cents was being protested. See note 8 *infra*. The public interest, as represented by the consumer interest, is not necessarily, or

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refund order. The Court felt that without such a limit on the refund obligation the Commission's grant of temporary authority was too vague to allow the producer to decide intelligently whether to accept the Commission's conditional grant and thereby commit its gas reserves to interstate commerce.

To the extent that our decision may be inconsistent with *Sunray* we are constrained respectfully to disagree with the latter. Moreover, it should also be pointed out that as a practical matter the producers in this case were relatively assured of being able to sell their gas without risk of subsequent refund at a price of 14.6 cents per Mcf., the price which PSC and the other consumer interests originally urged as the proper in-line price.

entirely, offset by the absence of an explicit refund condition in the temporary certificates, especially when those certificates contained the general conditions to which we have hereinabove referred. We do not attempt an enumeration of all equitable considerations involved. These are better left for at least initial Commission consideration in all the circumstances. We do hold, however, that the mere absence of the condition in the temporary certificates is insufficient to cast the full burden of excessive charges upon the consuming interests. There must be, with the assistance of the parties, a broader and more penetrating analysis and consideration of the factors pro and con a refund, and its amount or extent, in arriving at an equitable conclusion.

The refund issue requires further development and fuller consideration of the equitable factors other than those thought to flow from the mere absence of an explicit refund condition in the temporary certificates.

Nos. 17627 and 17859 affirmed.

Nos. 17382 and 17628 remanded for further proceedings consistent with this opinion.

APPENDIX B

Docket Nos. G-18638, *et al.*

Opinion No. 382

OPINION AND ORDER ISSUING CERTIFICATES OF PUBLIC CONVENIENCE AND NECESSITY

(Issued August 30, 1962)

SWIDLER, Chairman:

This proceeding, arising under Sections 7(c) and 7(e) of the Natural Gas Act, involves applications for certificates of public convenience and necessity for the sale of gas by a group of producers in Texas Railroad District No. 4, located in the southern tip of Texas. The producers propose to sell gas at various prices up to 18 cents per Mcf to South Texas Natural Gas Gathering Company, which, in turn requests certificate authorization to build additional facilities and to sell the gas at 20 cents per Mcf to Transcontinental Gas Pipe Line Corporation (Transco), also an applicant with respect to certain facilities. The Duval County Joint Venture, composed of Coastal States Gas Producing Company and Southern Coast Corporation, proposes to purchase additional gas at about 12 cents per Mcf and sell it to South Texas at 15 cents per Mcf. Some of these proceedings are before us for the second time after we granted rehearing of our order of November 22, 1960, in *Texaco, Inc.*, 24 FPC 979, where we issued certificates to Transco, South Texas, and a number of producers in the first phase of the contemplated expansion. After the second hearing the proceedings are before us upon exceptions to the examiner's decision issued January 25, 1962. The principal issues are whether the producer prices are proper, whether South Texas and the Joint Venture are pipeline companies within the meaning of the Commission's Regulations, and whether the 20-cent rate of South Texas to Transco and the 15 cent rate of the Joint Venture to South Texas are justified.

By contract of February 17, 1959, Transco was to purchase from South Texas at least 50,000 Mcf of gas per day at 14.65 psia and was to have the right to take up to 70,000 Mcf of gas per day (known as the first phase). On the first and second anniversaries of first delivery the daily contract minimum and maximum quantities were to be increased each year by an additional 50,000 Mcf per day and 70,000 Mcf per day (known as the second and third phases). The contract provides for an initial price of 20 cents per Mcf, to be increased one cent each 5 years from the date of first delivery. Transco has agreed to reimburse South Texas for three-fourths of any new or additional production or severance taxes, if such are levied, during the term of the agreement.

In its application Transco sought a certificate authorizing the construction of a pipeline 28.9 miles long extending from a connection with South Texas at a point in La Salle County, Texas, to a point on Transco's 24-inch line at the Tilden ga treating plant in McMullen County, Texas, and an additional compressor station. These facilities have been constructed under a temporary certificate, and Transco has been purchasing gas under the first phase since December 12, 1959 and under the second phase since February 14, 1961. As in the earlier hearings no opposition was expressed to Transco's proposal, although the Public Service Commission of New York (PSC) requested a finding that there have been no claims that Transco's favored-nation contract clauses have been "triggered". The examiner concluded as did the Commission in the previous proceeding (24 FPC 979, 984-985) that a finding with respect to triggering was not necessary. As stated in the prior order, Transco showed that it would be unwilling to pay a higher price even if triggering were not a factor and while this left the seller with the contractual option to terminate, the seller could not do so without abandonment proceedings before this Commission.

As stated in our prior order, "Transco's connection with South Texas has been constructed under a temporary certificate, and Transco has been purchasing gas since December 12, 1959. There is no issue raised with respect to the engineering, financial or economic feasibility of Transco's project or the need of its markets for gas."

South Texas, which is a wholly-owned subsidiary of Coastal States Gas Producing Company, previously owned and operated a natural gas system consisting of approximately 108 miles of pipeline extending north from the Rio Grande to a point in Jim Wells County. On July 2, 1959, under the "producer" regulations, South Texas filed its present application. The facilities were to consist of 195 miles of pipeline extending from South Texas' existing line in Brooks County to the point of interconnection with Transco in La Salle County, lateral lines in Zapata, Hidalgo, Starr and Webb Counties, gathering lines in various fields, and a compressor station. South Texas has constructed the facilities and is delivering gas to Transco under a temporary certificate. No question has been raised in the exceptions as to the engineering, financial or economic feasibility of the project.

Joint Venture owns about 100 miles of gathering lines in Duval and Webb Counties, Texas, and South Texas operates these lines for the transportation and delivery of gas destined for Transco.

The producer applications here seek certificate authorization to sell gas to South Texas. Certain of the applications for certificates were previously granted by the Commission; the remaining are additional and were filed in connection with amendments to South Texas' and Joint Venture's "original applications" to implement Transco's second phase quantity deliveries.[1] By order of May 11,

[1] On February 14, 1961, the Commission granted South Texas temporary authorization to sell the second phase increment.

1961, the Commission severed the applications of 52 producer applicants involved in the prior hearing. Their proposed prices were 14.5 cents per Mcf or less, and no controversy remained with respect to granting these applications.

In its first order of November 22, 1960, 24 FPC 979, the Commission found that the prices proposed by the producer applicants, ranging from 9 cents to 17 cents per Mcf at 14.65 psia, were "in line". The Commission was unable to determine whether the price spreads as proposed by South Texas and the Joint Venture were consistent with the public convenience and necessity but, in order to protect the consumers, required that the certificates issued to them be conditioned so as to require that, two years after the start of deliveries on December 12, 1959, these companies file cost of service studies acceptable to the Commission, accompanied by revised rate schedules, if necessary, reflecting such cost of service studies.

Upon application for rehearing by PSC, which argued that the prices used by the Commission were not comparable or were involved in litigation, the Commission granted rehearing. A second hearing was held from May 16, 1961, to June 26, 1961. Briefs were filed and the examiner issued his decision on January 25, 1962. In his decision he found that South Texas, but not the Joint Venture, should be classified as a pipeline. He determined that the cost of evidence in the record submitted by South Texas and the Joint Venture did not meet the requirements of the Commission's order of November 22, 1960, and required that cost of service evidence be submitted by both South Texas and the Joint Venture as called for by the Commission's prior order. He issued certificates to Transco, South Texas, the participants in the Joint Venture and the producers. He conditioned the certificate to South Texas so as to require refunds if the cost data to be filed showed the initial rate was excessive (but only amounts collected above

18 cents); with one exception[2] he did not condition the certificates issued the Joint Venture or the producers as to price because the proposed prices were below the current Texas District No. 4 area price of 18 cents. Exceptions to the examiner's decision were filed by PSC, Transco, Jake L. Hamon, Joint Venture, South Texas, a group of Eastern Interveners,[3] and our staff.

Although rehearing had been granted with respect to the 1960 order, South Texas and the Joint Venture submitted cost of service data on February 1, and 12, 1962, respectively. Meanwhile, on November 20, 1961, an application in Docket No. CP62-124 was filed by South Texas representing the third phase increase in the company's deliveries to Transco that would include an additional line in Hidalgo, Starr and Zapata Counties and would increase the minimum to 150,000 Mcf per day and the maximum to 210,000 Mcf per day. A permanent certificate was issued to South Texas in this docket on February 7, 1962, but conditioned so as to require that South Texas reduce its rate to Transco and make refund if this should be required by the principles employed by the Commission in these proceedings (Docket No. G-18907).

Producer Prices and Other Producer Issues

Basic here are the proper prices to be allowed the producers selling gas to South Texas and the Joint Venture. The proposed contract prices before us range from 14.7 cents to 18 cents at 14.65 psia as follows: one at 14.7 cents,

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[2] Jake L. Hamon, whose 18 cent price in Docket No. CI61-922, he said, was reached without arm's-length negotiations.

[3] Long Island Lighting Company, Philadelphia Electric Company, Public Service Electric and Gas Company and The United Gas Improvement Company.

12 at 15 cents, 12 at 16 cents, one at 16.50 cents,[4] one at 16.4965 cents,[5] 4 at 17 cents, and one at 18 cents (for Jake L. Hamon in Docket No. CI61-922). The examiner did not recommend the imposition of a price condition with respect to the producer prices except for Hamon, whose 18-cent price he would reduce to 16.5 cents for lack of arm's-length bargaining. The examiner cited the Policy Statement[6] as authority, noted that the Commission's area price standards were promulgated after due consideration, and referred to the staff's exhibits as showing an existing price level in the 16-17 cent range.

PSC excepts to the examiner's conclusions, requests the Commission to authorize producer sales at no higher than 14.6 cents per Mcf and asks that a corresponding reduction be made in charges of South Texas to Transco. PSC contends that the Policy Statement should not be involved in contested proceedings as an automatic determinant and that initial prices above 14.6 cents would be out-of-line and unlawful. The basis of PSC's contention is that most of the prices in District 4 above 14.6 cents are either involved in litigation[7] or were authorized for purchase by Coastal Transmission Corporation in connection with a single pre-*CATCO*[8] 1956 certificate decision, *Houston Texas Gas and Oil Corp.*, 16 FPC 118 (December 28, 1956).[9]

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[4] This is the Mokeen Oil Company price in Docket No. CI60-789 composed of a base price of 16.25 cents plus a dehydration allowance of .25 cents.

[5] This is the Texaco price in Docket No. CI61-961 at a base price of 15.2 cents increased to 16.4965 by reimbursements including a .25 cent dehydration allowance.

[6] Statement of General Policy No. 61-1, issued September 28, 1960, 24 FPC 818.

[7] *PSC* v. *FPC*, 295 F.2d 140, certiorari denied 368 U.S. 948.

[8] *Atlantic Refining Co.* v. *FPC*, 360 U.S. 378.

[9] Affirmed as *Florida Economic Advisory Council* v. *FPC*, 251 F.2d 643 (CADC), certiorari denied 356 U.S. 959.

The Eastern Interveners in their exceptions take a similar position. They point out that in the order on rehearing in *Coastal Transmission Corporation*, Docket No. G-18338, issued November 2, 1961, the Commission rejected contentions that under the Policy Statement it must issue permanent unconditioned certificates where the contract rates do not exceed the ceiling. They also point out that as in *CATCO* this proceeding involves contracts executed before the issuance of the Policy Statement so that the Commission must determine the "in line" price for the contracts at the time of their execution. They concluded that a price line of no more than 14.6 cents should be established for the area.

The only producer filing exceptions on prices was Hamon, who contends that if the Policy Statement is to be effective, a producer should be able in good faith to rely on the prices set forth in the Statement—at least until lawfully superseded. Other producers in their briefs took a position different from PSC and the Eastern Interveners. Texaco contended that its proposed 16.4965 cent price was not out of line and because it was below the 18-cent ceiling, it was entitled to an unconditioned permanent certificate. On the basis of the Policy Statement it further contended that producer regulation should be based on the reasonable financial requirements of the industry and discussed its financial evidence and the need for developing gas supplies. Continental also presented financial evidence, contended that the Policy Statement means that the Commission intends to certificate prices up to the announced guide levels without condition in the absence of compelling evidence to the contrary, and concluded that on the basis of the staff's evidence the proposed prices were in line, apparently relying on the earlier Coastal prices. Other producers, including Skelly, variously contended that the proposed prices should be certificated because they were below the Policy Statement ceiling, were "in line", were at arms-length, would not "trigger" other increases and were otherwise justified.

As in other cases our principal guide to the determination of a proper initial price for the producers is the Supreme Court's Opinion in the *CATCO* case. There the Court made it clear that we were not required to determine "just and reasonable" rates, but were required to scrutinize the proposed initial prices to determine whether they were supported by evidence showing them to be required by the present or future public convenience and necessity. The Court said that where "the proposed price is not in keeping with the public interest because it is out of line or because its approval might result in a triggering of general price rises or an increase in the applicants' existing rates by reason of 'favored nation' clauses or otherwise, the Commission in the exercise of its discretion might attach such conditions as it believes necessary".[10]

An important consideration in making our findings in this proceeding is the effect to be given our Statement of General Policy No. 61-1. This Statement was issued September 28, 1960 to assist in meeting the practical problems of regulating the prices of the independent producers pending competition of the various area rate proceedings. It sets forth price levels applicable to various areas in determining whether certificates for new sales should be conditioned upon acceptance of a lower price and increased rate filings should be suspended. The area price ceiling for Texas District No. 4, where the producer sales in this proceeding are made, was set at 18 cents per Mcf for initial service and 14 cents per Mcf for increased rates, both at 14.65 psia. However, as the language of the Policy Statement makes clear, the area ceilings are guidelines to future Commission action.[11] Our Policy Statement cannot effect an automatic approval of proposed rates, particularly where the contracts were entered into before the Policy State-

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[10] 360 U.S. at P. 391.

[11] See the *Phillips* case, *Wisconsin v. FPC*, ... F.2d ... (CADC. November 30, 1961), certiorari granted 369 U.S. 870.

ment.[12] We made this clear in *Coastal Transmission Corporation*, —— FPC ——, Docket No. G-18338, order of November 2, 1961, where we said:

> In their applications for rehearing, Baker, Superior, and Phillips contend that by not issuing unconditioned permanent certificates in those dockets in which their contract rates are at or below the appropriate area price guides set forth in Statement of General Policy No. 61-1, cited *supra*, we are in effect modifying if not repudiating our Policy Statement.
>
> Our actions here do not repudiate the Policy Statement. The price guides for initial service contained in the statement in effect constitute ceilings at which a proposed initial sale will, in the absence of otherwise compelling evidence, be certificated. The price guides do not constitute a floor to be used to raise proposed initial prices to the highest levels abstractly permissible thereunder. Obviously circumstances may exist which would compel the submission of evidence by the producer in support of rates at or below the appropriate area levels. Such circumstances we believe are present herein. For example, the challenge made to these producers' proposed initial prices coupled with the complete lack of any record by which to test the propriety of the initial prices proposed. Consequently, the deferral of final certification herein is in full accord and harmony with the tenor and explicit provisions of our Policy Statement.

Following the Supreme Court Opinion in *CATCO* we must determine the appropriate price "line" for District No. 4. This line should be determined as of the time the

[12] Of course, we are discussing here only the area ceilings promulgated in the Policy Statement without hearing. The effect to be given to area prices developed upon a record in an area proceeding is a different question.

contracts were made,[13] so that we should properly put greater emphasis on the calendar years 1958, 1959, and 1960. The most important evidence available for determining the price line is a study prepared by our staff (Exhibit 24) showing the provisions of contracts in District No. 4 dated 1955 and later. Because proceedings related to lower priced sales were severed and certificates have already been granted for them, the study shows only contracts at prices of 14 cents per Mcf and higher. However, we may take notice that we have granted certificates for sales in District No. 4 during the three years in question at prices ranging down to 6 cents per Mcf, usually for small volumes.

Tabulating the staff's evidence with respect to the three years 1958-1960 we find the producer contracts and estimated first month's deliveries distributed among the initial price categories as follows:

[13] *See Continental Oil Company, et al., CATCO . . . FPC . . .* Opinion No. 351, Docket No. G-11024, *et al.*, issued January 22, 1962.

Price	No. of Contracts Under Permanent Certificates [a]	Estimated First Month Volumes	No. of Contracts Under Temporary Certificates [b]	Estimated First Month Volumes
		(Mcf)		(Mcf)
14	26-(1)	1,289,600 [c]	7-(4)	365,800
14.25			1	5,053
14.4	1	7,500		
14.5	16-(1)	1,214,625 [d]	2-(1)	180,000
14.6	2	166,000	2-(2)	86,350
14.8	2	80,550	2-(1)	102,000
15.0	1	116,370	3-(2)	133,710
15.5			1-(1)	45,000
16.0	12-(11)	480,620	6-(2)	1,086,000
16.5	7-(7)	233,250	2	193,080
17.0	4-(3)	494,500	1-(1)	12,371
17.24			17-(1)	1,691,624
18.0	5-(5)	867,810	7	970,920
18.23			6	535,565

[a] The parenthetical numbers in the various price categories for permanent certificates represent those of the total shown challenged and on remand in *PSC* v. *FPC*, 295 F.2d 140 (CADC, June 15, 1961) some of which have been changed to temporary certificates in *Coastal Transmission Co.*, ... FPC ..., Docket No. G-18338, November 2, 1961, and in *Hassie Hunt, Operator, et al.*, Docket No. G-19115, November 2, 1961.

[b] In the column for temporary certificates, the parenthetical number indicates those of the total shown subsequently made permanent at the indicated prices. Of the five temporary certificates made permanent at prices above 15 cents three were permanently certificated *prior* to remand in *PSC* v. *FPC*, *supra*. McWood Corporation with a price of 15.5 cents was granted a certificate on August 7, 1961, in Docket No. C161-259. *Coastal States Producing Company*, with a price of 16 cents was granted a certificate on May 1, 1962, in Docket No. G-20127. This sale, while comparatively large in amount (450,000 Mcf for the first month), related to surplus gas originally to be delivered only for a six-month period.

[c] This total includes three separate monthly estimated deliveries of 180,000 Mcf each and two of 90,000 Mcf.

[d] This total includes separate monthly estimated deliveries of 150,000, 280,500, and 213,500 Mcf.

Several conclusions can readily be drawn from an inspection of the above figures and the evidence itself. Looking at the permanent certificates it appears that almost all contracts above the 15-cent level were the subject of litigation.[14] Specifically, the Commission's orders[15] granting certificates were remanded in *P.S.C.* v. *F.P.C.*, 295 F. 2d 140 (CADC, June 15, 1961) certiorari denied 368 U.S. 948 where the court found that the Commission had erred in failing to permit PSC to intervene. While the Court did not determine what the proper level of the rates should have been, nevertheless the rates involved in this court proceeding must be considered under a "cloud" for the purpose of using them to establish a price "line", for it was the purpose of PSC, in petitioning for intervention, to oppose the granting of certificates at those prices. *United Gas Improvement Co.* v. *F.P.C.*, 283 F. 2d 817 (CA9), certiorari denied 365 U.S. 881.[16] In that case the

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[14] One at 17.0 cents, not subject to litigation is the large sale (480,000 Mcf in the first month) by *Valley Gas Transmission Inc.* in Docket No. G-19618. This is a gathering company sale and is not comparable to sales by producers, for Valley purchases all the gas which it sells. In this docket it was given a certificate (25 FPC 233) to sell gas to Tennessee Gas Transmission Co. in District No. 4 at 17 cents, which it would purchase from various producers at 14 cents. The other at 16.00 cents is a small producer sale (15,500 Mcf in the first month) by *V. F. Neuhaus* in Docket No. G-18862.

[15] *Texas Illinois Natural Gas Pipeline Company, et al.*, Docket No. G-14829, *et al.*, intervention denied March 26, 1959, certificates issued 22 FPC 979, Dec. 1, 1959; *Peoples Gulf Coast Natural Gas Pipeline, et al.*, Docket No. G-19086, intervention denied March 21, 1960, certificates issued 24 FPC 1, 106, July 29, 1960; *Coastal Transmission Corp., et al.*, Docket No. G-18338, *et al.*, intervention denied March 3, 1960, certificates issued in *The Ohio Oil Co., et al.*, Docket No. G-17896, *et al.*, September 19, 1960.

[16] See also *United Gas Improvement Co.* v. *FPC*, 290 F.2d 133 (CA5), certiorari denied, 368 U.S. 823.

Court said that when "an order certificating an initial rate is under court or Commission review" it "does not provide a reasonably reliable basis upon which to predicate a price line" Even where the review concerns only the right to intervene, prices subject to such review "ought not to be considered in fixing a price line." Thus we must eliminate from the discussion the prices involved in the *P.S.C.* v. *F.P.C.* remand. With one minor exception,[17] this leaves no produced prices under permanent certificate above 15 cents at the time the record was closed in this proceeding as shown by the second column of the table

The table above also shows prices under temporary certificates ranging from 14 cents to 18.23 cents, including a few that have subsequently been made permanent;[18] and staff's evidence, but not the table, also sets forth prices under permanent certificates for the years 1955, 1956 and 1957 relating to sales at 16 to 17 cents to Coastal Transmission Corporation. Both groups of prices fall under a corollary principle stated by the court in the *U.G.I.* case, supra (283 F. 2d at P. 824), as follows:

> We go further and express the view that where a substantial number of certificated prices are thus under court or Commission review, like prices in the same area though not currently under review ought to be regarded as suspect. In such circumstances it would seem that such similar prices ought not to be relied upon in fixing a line except upon evidence and findings to the effect that they are not subject to the same infirmities which are under test in the pending proceedings.

The prices under temporary certificates fall into approximately the same price categories as those subject to review

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[17] See footnote 14.

[18] See footnote b in table.

and thus under the court's reasoning must be regarded as suspect. The applicants have not shown that the prices under temporary certificates [19] are not subject to the same infirmities as those which are under test in the *Skelly* proceeding pending before us. Specifically, no attempt has been made to show that these suspect like prices were themselves "in line" at the time they were made. Furthermore, we do not think that prices under temporary certificates are as persuasive as the prices under permanent certificates, because temporary certificates are issued informally, *ex parte* and necessarily without time for full investigation. The granting of temporary certificates is a summary matter to meet an emergency. *American Liberty Oil Co.* v. *F.P.C.*, 301 F. 2d 15 (CA5, March 30, 1962), No. 18827; *Huber Corporation* v. *F.P.C.*, 294 F. 2d 568 (CA3, 1961).

Likewise, the record does not show that the Coastal 1956-1957 sales were not subject to the same infirmities as those in the present proceeding. There is no showing that these earlier prices, which were markedly higher than any jurisdictional sales ever made in Texas District No. 4, established a valid new line for sales to established pipelines in the District.[20] On the contrary, as the table shows in the

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[19] Including those subsequently made permanent.

[20] The earlier Coastal sales were made to a new company that had neither been given a certificate nor was yet in operation, so may have resulted in higher prices than would have resulted from contracts with an established pipeline. Moreover, the Eastern Seaboard interveners were excluded from the hearing for reasons subsequent court decisions have shown were invalid, and the New York Commission's protest to the high rates as "out of line" were rejected by the Commission on the basis that the record did not show in effect whether they were in line or not (apparently on the erroneous assumption that this was a burden for the interveners rather than the applicants to meet). *See Houston Texas Gas & Oil Corp., et al.*, 16 FPC 118, 141-142, 17 FPC 303, 310.

succeeding three years the great majority of sales (including almost all not procedurally defective) were at less than 15 cents.

Returning to the evidence summarized in the table, we may note that there are a number of contracts involving substantial volumes of gas at the 14.0 cent and 14.5 cent price levels not subject to litigation. While the evidence shows only two contracts at 14.6 cents, two at 14.8 cents and one at 15 cents, certain of the temporary certificates at these levels have subsequently been made permanent in other proceedings so that there result 4 contracts at 14.6 cents with estimated volumes of 252,350 Mcf in the first month, 3 contracts at 14.8 cents with volumes of 120,550 Mcf and 3 contracts at 15.0 cents with volumes of 238,080 Mcf. As can be seen, there is but one contract relating to a moderate volume at 15.5 cents. The record shows that while the volumes vary among the individual contracts, the proposed sales are not of such high volumes that they are not comparable to these already certificated, nonlitigated sales at 15 cents or below. Based upon the evidence we conclude that the price line prior to September 28, 1960 was 15 cents per Mcf and that any price above this level is out-of-line.

As already indicated Texaco and Continental have introduced additional economic and financial evidence to justify their proposed prices of 16.4965 cents and 16 cents respectively. Texaco's evidence is designed to show the replacement cost of the gas which it sells. It presents industry-wide cost trends and also data on the costs of replacing gas consumed for the United States as a whole and for the Texas Gulf Coast area, using a variety of statistical sources and employing a number of estimates based on judgment. To some extent the results depend on the future demand for gas, for Texaco introduces a factor so as to include not only the cost of replacing the present gas consumed but also additional gas necessary to meet future needs. Thus under Texaco's theory the present consumer would,

in effect, be burdened not only with the cost of the already-discovered gas he now consumes, plus at least some of the cost of replacing it, but also with costs associated with the discovery of additional volumes of gas based upon future demand trends. From the country-wide and area-wide data Texaco then attempts to draw similar conclusions with respect to its own financial needs by comparing its exploration and drilling costs with the industry figures.

In support of its presentation Texaco quotes the *Phillips* case [21] which states in effect that our ultimate objective will be the determination of fair prices for gas based on the reasonable financial requirements of the industry. It argues that by "reasonable financial requirements" we mean the revenues required by the producing industry from sales of natural gas in order to provide funds sufficient to search for, develop and produce gas supplies adequate to meet the continuing demands of the public for gas. In our opinion these observations and Texaco's evidence are not germane to this certificate proceeding. The principal criterion that should be employed here is whether the proposed prices were "in line" at the time of contract execution as required by the Supreme Court's *CATCO* opinion.[22] Texaco's observations and evidence may have an important bearing on determinations to be reached in an area rate proceeding, or might be relevant in an individual company rate case although they fall short of showing Texaco's costs. However, we do not think it necessary or appropriate in a certificate proceeding to consider evidence of area costs or financial requirements, or of individual company costs or financial requirements. Any such approach is of limited utility [23] and leads to complicated, long-drawn-out proceedings, detrimental to the public.

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[21] 24 FPC 537, 547.

[22] *Atlantic Refining Co.* v. *PSC*, 360 U.S. 378.

[23] See *Continental Oil Co., et al.*, ... FPC ..., Opinion No. 251, Docket No. G-11024, *et al.*, issued January 22, 1962.

Questions concerning the cost of replacing present reserves, and more particularly whether such costs should be borne by present customers or by venture capital are not questions to be decided in a section 7 certificate proceeding. Rather, they are central questions to be decided in area rate proceedings.

We therefore hold that cost of service and financial requirements evidence normally is not relevant in producer certificate cases and that the initial price in such proceedings shall be determined by the "in line" price in the area at the time the producer contract in issue was executed and by our guideline ceiling price for the area. We do not mean to foreclose the possibility that a producer may present compelling circumstances in a particular proceeding to justify a higher price, but we wish to emphasize that with the guidelines herein established the price issue in certificate cases should be handled expeditiously and that before any evidence which would customarily be presented in establishing a just and reasonable rate can be admitted in evidence, a convincing showing must be made that such evidence is essential to the just disposition of the price question.

Obviously, we cannot permit every individual certificate case to be converted into a full-blown rate case; the proof in this proceeding demonstrates the lack of utility of a limited cost of service presentation. The evidence does not show the cost of present reserves and consequently does not indicate the price necessary to cover such costs and provide a return which will attract sufficient risk capital to undertake the exploration and development necessary to replace present gas reserves.[24] More generally, the

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[24] Compare *Panhandle Eastern Pipe Line Co.* v. *FPC*, ... F.2d ..., (CADC, June 30, 1962) No. 16583 where in a rate case the court upheld the Commission in refusing to base rates on field prices or hypothetical development costs.

evidence does not demonstrate the "financial requirements" of Texaco or the other producers in this proceeding, for the relation of individual needs to those of the industry in the country as a whole or in the area is not shown by the limited comparisons made. To correct those defects would require a complete rate case, which we have found not warranted in a certificate proceeding.

Continental strives to support its 16 cent price in the Javelina Field by reference to its evidence showing that from 1946 to 1963 it would spend more than twice as much as it had realized or would realize. In fact, it said it would have to receive $2.78 per Mcf in order to recoup its cash outlay. Apart from the question of the type of evidence appropriate in a certificate proceeding such narrowly limited cost data would not form a proper basis for appraising financial requirements. *See Socony Mobil Oil Company*, —— FPC ——, Docket No. G-13780, February 9, 1962.

Therefore with respect to all of the producer prices contained in contracts entered into prior to September 28, 1960, the date of issuance of the Commission's Statement of General Policy No. 61-1, we conclude that the "in-line" price was 15 cents per Mcf, including all reimbursements and charges, and that certification of all prices above this rate are not in the public interest and would not serve the public convenience and necessity.

While we shall therefore condition the certificates of the producers having such contracts upon their acceptance of the 15 cent in-line price, we do not believe we should also do so with respect to the four contracts in issue here which were entered into after September 28, 1960, at prices at or below the 18 cents per Mcf established as the guideline price for Texas Railroad District No. 4 in the State-

ment of General Policy.[25] For the record in this case does not focus upon the effect, if any, which should be given to the prior establishment of the 18-cent area ceiling upon the determination of the appropriate price at which we should issue permanent certificates for these contracts. And we take judicial notice of the fact that at least 21 other temporary certificates (and one permanent certificate) have been issued without price condition for sales in Texas Railroad District No. 4 contracted for since the issuance of the policy statement at prices between 15 cents and 18 cents per Mcf. Moreover, the contract dates for some of these certificates precede the contract dates of the four post-policy-statement temporary certificates in issue here.

In our opinion, therefore, it would not be in the public interest to issue permanent certificates requiring those producers whose applications for certificates for sales, contracted for at prices at or below the ceiling which had previously been set in the policy statement, happened to have been consolidated in this proceeding (because their sales were to South Texas or Joint Venture), to accept 15 cents per Mcf while all the others continue to collect higher prices. We are, by separate order, severing these four applications for permanent certificates from this proceeding and consolidate them into a new hearing on their per-

[25] These contracts are:

	Docket No.	Price	First Month's Production (Mcf)	Date of Contract
Katz	CI61-627	17¢	75,000	10-17-60
Hamon	CI61-922	18¢	58,333	11-21-60
Sun	CI61-956	17¢	300,000	12- 1-60
Texaco Inc.	CI61-961	16.4965¢	9,280	12- 1-60

The action taken here obviates the need for determining in this order whether the Hamon sale was or was not made at arm's length, and we do not adopt the examiner's discussion of this point.

manent certificates, together with all of the other holders of temporary certificates which have been issued for sales in Texas Railroad District No. 4 contracted for between September 28, 1960, when the existing 18-cent area ceiling was adopted and the effective date of the amended area ceiling in this area which we are adopting simultaneously herewith. In such a hearing all of such parties will have an opportunity to show whether the appropriate price at which they should be permanently certificated should be limited by the 15-cent per Mcf price which we have found was the in-line price as of September 28, 1960, the 16-cent per Mcf price we are adopting as the ceiling price applicable to all future contracts in this area (pending completion of the governing area price hearings), or the 18-cent per Mcf price established on September 28, 1960.

Unlike the situation in *CATCO* where all of the unconditioned price certificates by which gas was dedicated to interstate commerce were either subject to timely court review because challenged and appealed or (in one case) granted pending such review, the producers here have been operating, pending this hearing on their permanent certificate application, pursuant to effective temporary certificates containing no price condition, the validity of which have never been challenged on appeal. Under these circumstances we believe that there is no basis for ordering refunds for the period, prior to the effective date of the permanent certificates being issued herewith, during which the producers were receiving the higher prices unconditionally authorized in their temporary certificates.

The examiner did not accept a staff recommendation that all of the produger sales be conditioned to limit the take-or-pay requirement to 80 percent of the contract quantity and that the daily contract quantity be limited to one Mcf for every 8,000 Mcf of originally dedicated reserves. The examiner was of the opinion that the staff recommendation was inconsistent with our allowance of prepayments for

gas by the purchaser in a rate proceeding.[28] While we may allow such prepayments, such an allowance does not require us to approve take-or-pay provisions in producer contracts. This matter, however, is the subject of our Notice of Proposed Rule Making of May 22, 1961, in Docket No. R-199, so that it would be inappropriate to pass upon it now. However, we shall make the producer certificates issued herein subject to the results of the rule-making proceeding.

The examiner rejects the contention of the staff and agrees with Mokeen Oil Company that a provision in its contract does not constitute an indefinite escalation contrary to Section 154.93 of our Regulations. This provision is to the effect that if Mokeen has reserves in excess of the 160 billion cubic feet dedicated to the contract it has the option to dedicate these additional reserves to the contract, but if it elects not to dedicate the reserves then South Texas shall have the option "to purchase said excess gas under a separate contract at a price per Mcf which is equal to the average of the two highest prices being paid by gas transmission companies" in the field. We are not at this time determining the question as to whether the dedication of additional reserves to the contract shall constitute a dedication of reserves under the original contract or shall constitute an initial dedication of reserves. We shall deal with this question when it is presented.

South Texas and the Joint Venture

We now turn to the issues relating to South Texas and the Joint Venture. The question whether these two enterprises should be treated as independent producers or pipelines affects the kind of applications, annual reports, and rate schedules they will be required to file. In our prior

[28] See *Michigan Wisconsin Pipe Line Co.*, ... FPC ..., Opinion No. 353, Docket No. CP61-102, issued March 7, 1962. The allowance of prepayments in South Texas' rate base would have a *de minimis* effect in this proceeding.

order the Commission concluded South Texas should be treated as a pipeline for the purpose of examining the validity of its rates, and that the Joint Venture should be treated the same way although it was an independent producer within the meaning of the definition in our Rules (Section 154.92(a) as of that time). In the present proceeding the examiner determined that South Texas was a pipeline and the Joint Venture was a gatherer and producer.

As to South Texas, the examiner noted that it is engaged predominantly in the transportation of gas for distances of 100 miles or more in interstate commerce. He placed particular reliance on the Commission's order in *Ben Bolt Gathering Company, et al.*, 26 FPC —, Docket No. G-20032, *et al.*, December 12, 1961.[27] In that case the Commission found that Ben Bolt would carry gas 26 miles in a pipeline extending from connections with its suppliers at central field points to two points of sale to Natural Gas Pipeline Company and held that Ben Bolt was an interstate pipeline within the meaning of the regulations. At that time section 154.91 defined "independent producer" to include those engaged in production or gathering but "not primarily engaged in the operation of an interstate pipeline". The present regulation reads as follows:

> An "independent producer" as that term is used in this part means any person as defined in the Natural Gas Act who is engaged in the production or gathering of natural gas and who sells natural gas in interstate commerce for resale, but who is not engaged in the transportation of natural gas (other than gathering) by pipeline in interstate commerce.

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[27] The examiner noted further that by letter of September 7, 1961, rejecting South Texas' filing in Docket No. CI62-115 the Commission had already found the company to be a pipeline. This letter was limited to a requirement that South Texas file certificate applications in the full pipeline form rather than in the summary independent producer form.

South Texas receives gas from a number of fields, some near the Mexican border in Hidalgo County and others located in Starr, Brooks, Jim Hogg, Zapata, Webb and Duval Counties. Certain of its facilities, particularly those near the border, may be said to perform a gathering function in that they bring the gas to a central point. However, the South Texas line extending from the border through the various counties to the point of delivery to Transco in La Salle County performs the function of transporting natural gas that has already been gathered. Therefore, South Texas is a pipeline company within the meaning of Section 154.91(a) of our Regulations.

Both South Texas and Transco object to classification of the former as a pipeline. They contend variously that this would require that South Texas file a pipeline type of tariff, and this would, in turn, require that South Texas pool all sources of supply for the performance of its contracts with Transco and Natural Gas Pipe Line. Further, this would free South Texas from the restrictions of its contract and enable it to file a rate increase at any time it could be justified. These contentions are not valid under our Regulations. Under section 154.52 providing an exception to form and composition of a tariff the Commission "may permit special rate schedules to be filed in the form of an agreement in the case of special operating arrangements such as for exchange or transportation of natural gas". We think it desirable because of the special service rendered by South Texas that the rate restrictions of its contracts and the dedication of gas to its customers be preserved. Therefore, South Texas should meet the requirements of our Regulations with respect to pipelines by filing its contracts as special rate schedules under section 154.52.

The Joint Venture, on the other hand, is in a different position. Its line in Duval and Webb Counties does in effect bring gas to a central point, situated on the line of South Texas. The examiner found that it is engaged pre-

dominantly in gathering gas in aid of the selling producers and that it is a gatherer under the *Ben Bolt* order and is thus an independent producer. No exceptions were filed on this point, and we agree with the examiner's conclusion.

The proper rate for the South Texas sale to Transco is an important issue in these proceedings, for this rate reflects the producer prices and the costs of South Texas and the Joint Venture. South Texas' cost of service presentation, as discussed below, is based on its average purchased gas costs from the producers, which has risen with each succeeding phase of its expansion. Conditioning the producer certificates that are above 15 cents (with the exception of the four dockets referred to at page 15, *supra*) will, of course, lower the average cost of purchased gas and will require a lower price to Transco.

A basic question is whether the South Texas evidence in support of its rates is adequate. In our previous order of November 22, 1960, on which we granted rehearing, we required that South Texas, after the first two years of operation,[28] "file detailed data setting forth the cost of service upon the basis of actual experience." At the second hearing South Texas showed plant investment and income earned in the twelve months ended February 28, 1961. This includes first phase gas (50,000 Mcf per day) plus some second phase gas since temporary authority for the second phase was granted February 14, 1961. There resulted a total company rate of return of 5.90 percent and 5.61 percent applicable to the sale to Transco. South Texas also presented an adjustment to this cost computation to reflect additional costs and revenues anticipated as a result of the second phase gas. It shows a company-wide return of 5.90 percent, but 5.77 percent return applicable to the Transco deal. South Texas also filed an economic feasibility study in connection with its second phase application

[28] Deliveries under the first phase began in December of 1959.

in Docket No. G-18907, and this study was made a part of the record here. The study was a three-year forecast of earnings from the second increment of gas delivered to Transco showing a 6.7 percent return in the third year. After considering the adequacy of the evidence the examiner required that South Texas (and Joint Venture) submit the detailed cost of service data required by our previous order.

While the cost evidence referred to above falls short of a complete presentation, South Texas did file cost of service studies on February 1, 1962, purportedly in compliance with our order of November 22, 1960, but after the close of the record in this proceeding. South Texas stated it was using actual operating experience for its fiscal period ending June 30, 1961, with adjustments necessary to reflect the third year of operation after December 12, 1959; *i.e.*, 1962. Normalizing deferred taxes, and using contract minimum volumes and a 7.34 percent rate of return, the company arrived at 20.4 cents per Mcf for the total cost of service and 20.7 cents per Mcf applicable to Transco. While this latest study is not part of the record, it is supported generally by the prior cost studies, and we will admit it as evidence subject to objection.[29]

Coming to the substantive questions in the cost of service studies we find that the only factor in controversy that would make a material difference in cost level is the volume of gas used. The examiner found that if only minimum quantities were delivered, no reasonable adjustment could bring the cost of service materially below 20 cents. However, he said, there is no evidence that any greater quantity than the minimum is being delivered under either phase of the contract.

[29] PSC in its exceptions did not object to the price spread between South Texas' purchases and sales, but requested that reductions in the producer prices be reflected in the South Texas price to Transco.

The staff contends in its exceptions that the evidence does not support the use of minimum contract volumes. It points out that the South Texas contract with Transco provides for an adjustment of the minimum quantities depending on the recoverable reserves. On the basis of evidence of reserves the staff finds in the third phase an adjusted minimum of 174,103 Mcf per day instead of 150,000 Mcf per day.

In its exceptions South Texas cites testimony that, at least with respect to the first two phases, deliveries have been at the minimum contract level. Furthermore, it says, without citing the record, that it has agreed with Transco that the reserves do not exceed those required for the contract minimum of 150,000 Mcf per day, as of December 12, 1961, and no further contract reserve determination is provided until December 12, 1963. In its February 1, 1962 cost filing, South Texas refers to Transco's application in Docket No. CP62-86 which shows that South Texas will deliver no more than the contract minimum for the next twelve years. In any case it appears from this cost filing that it would take an increase in volume from the minimum of 150,000 Mcf per day to 179,400 Mcf per day to decrease the cost by only one-half cent.

While recognizing that volume is the only significant factor in the contract rate, the examiner concluded that South Texas as a pipeline should be allowed a rate of return of six percent. South Texas in its exceptions contends that this finding is unsupported by evidence and without explanation and advocates a rate of return of 7.3 percent based upon a 10 percent allowance for common equity.

In its recent cost filing South Texas arrived at a 7.34 percent rate of return using a debt ratio of 68.7 percent, a cost of debt of 6.13 percent and an allowance for common equity of 10 percent. We may note that on the basis of the cost of service filing a recomputation of South Texas' costs using a 6 percent rate of return and no allowance for taxes

would reduce the unit cost by only one cent from 20.7 cents per Mcf to 19.7 cents per Mcf.

On the treatment of Federal income taxes the examiner referred to the Commission's previous opinion, the cost evidence submitted, and the Staff's brief, and disallowed the claimed cost of Federal income taxes. In its brief, staff contended that because South Texas and its affiliated companies filed a consolidated return and South Texas had not paid Federal income taxes for the years 1959 and 1960, there seemed little justification for making provision for such taxes in the cost of service. On the other hand, South Texas points out that the greater part of the tax allowance shown in the cost of service presented by it relates to deferred income tax resulting from the use of liberalized depreciation tax accounting under Section 167 of the Internal Revenue Code. It also contends that its customers should not benefit from the losses of other companies, incurred before it was in business.

The question of the treatment of deferred taxes is before us in *Alabama-Tennessee Natural Gas Company*, Docket No. G-5471, *et al.*, and has been set for oral argument. The question of the effect of losses of affiliated companies on a consolidated tax return is before us in *Cities Service Gas Company*, Docket No. G-18799. While relevant to a degree, the tax question is small and need not be decided here. It appears from South Texas' February 1, 1962 cost filing that elimination of the entire tax allowance would reduce the cost of service to Transco by only .6 cents from 20.7 cents to 20.1 cents.

On the basis of the evidence we conclude that assuming the producer prices were proper, South Texas' 20-cent rate to Transco was proper. Since the effect of our order will be to decrease South Texas' purchased gas costs, we shall require South Texas to file an amended rate schedule reflecting this reduction in purchased gas costs.

The Joint Venture proposed a price of 15 cents per Mcf to South Texas. The examiner was of the opinion that its cost evidence submitted February 12, 1962, did not meet the requirements of the Commission's November 22, 1960, order, for no allocation of investment or operating costs was made for the use of the system to transmit gas purchased independently by Southern Coast Corporation. However, he treated its proposed price as justified because it was below the 18-cent ceiling in Texas Railroad District No. 4. For the same reason he did not find it necessary to determine a rate of return. He reached the same conclusion on Federal income taxes as in the case of South Texas.

The Joint Venture takes exception to the need for an additional allocation of its costs. It points out that there have been no sales to Tennessee on the part of the Joint Venture, and that the sale by Katz Oil Company to Southern Coast Corporation is actually a sale to the Joint Venture since under the Joint Venture agreement purchases of gas by either party to the Joint Venture are for the benefit of both and belong to the Joint Venture. The Joint Venture also contends that if its rate should be measured by the Policy Statement, there is no reason to make a finding on Federal income taxes, but if such a finding is made it should be consistent with respect to the Commission's prior holdings on liberalized depreciation.

Cost evidence presented by the Joint Venture based on the twelve months ended February 28, 1961, showed 7.01 percent return on the rate base allocable to the South Texas sale. However, the Joint Venture contended that operations during this period were not typical, since there was an abnormal volume of sales during this period in order to enable South Texas to meet its obligations before it could make connection with other supplies. Normalizing its costs for the same period the Joint Venture showed a return of only 3.39 percent on its service to South Texas.

In its February 12, 1962 cost filing the Joint Venture uses an 11 percent return and arrives at a unit cost of 20.9 cents. This was based on actual operating expense for 1961 adjusted to the test year 1962, in which it said there would be a substantial reduction in volumes. It appears that if the return were reduced to 6 percent and the Federal income tax eliminated, the unit cost would be 18.3 cents per Mcf for 1962, but only 15.4 cents per Mcf for 1961.

As explained above in connection with the producer prices the fact that the Joint Venture's price of 15 cents is below the Policy Statement area ceiling does not automatically justify it in these proceedings. However, we think that the available cost of service evidence, which is supported by the February 12, 1962 cost filing, shows that the proposed 15-cent price appropriately serves the public convenience and necessity and is justified.

A few words should be added, in conclusion, with respect to the attached statement of Commissioner Ross. His specific disagreement with our holding is limited to our failure to determine on this record the in-line price with respect to the four post-area ceiling price contracts which had been consolidated for hearing here with a much larger number of certificate applications involving contracts entered into prior to that date. This action, he suggests, involves an unwarranted reliance upon Commission expertise, as well as improper delay in affording producer and intervener alike an opportunity to test the Commission's ceiling prices by the hearing process contemplated by the statute. But as we made clear, *supra*, our determination to sever these four relatively small applications and to consider the price at which they should be permanently certificated in a new proceeding, together with the other temporary certificates issued in Texas District No. 4 since the establishment of the 18-cent ceiling price, resulted not from any unwillingness to expose these parties to the test of a hearing record, but rather from our conviction that the present record

provided an inadequate basis for determining the proper initial price for these contracts.

The precise question of the weight to be given in a certificate case to the area price in effect at the time a producer contract is executed has not previously been an issue before this Commission. The *CATCO* case and our other recent certificate decisions all involved contracts executed before area prices were announced. The record in this proceeding also focused on the question of the in-line price for the period prior to the announcement of area ceilings. It contained inadequate information for evaluating the effect, if any, of the Commission's enunciation of an 18-cent ceiling upon the in-line price in the area at the time the four post-area ceiling contracts were made.

We do not suggest that the Commission's announcement of ceiling prices as a guideline for conditioning certificates and suspending rate increases necessarily had the effect of raising the in-line price to that level but the Commission is not prepared in advance of a hearing on the issue to say that its own ceiling prices are entitled to no weight in determining the initial price under contracts executed after the ceiling prices were put into effect.

Neither can our actions here be characterized as substituting expertise for the hearing process. We have rejected, after hearing, the contention that the establishment of the 18-cent ceiling in September 1960 fixed that price as the proper in-line price in Texas Railroad District 4 as of that date; and we have placed in the hearing crucible the issue of the effect of the ceiling upon subsequent contracts—a hearing which can be concluded promptly under the new guidelines enunciated in this opinion for determining the initial price.

If we understand the implications of Commissioner Ross' statement, it would destroy the interim price ceilings which have been effective in holding the line against further

increases in producer prices pending determination of just and reasonable prices in the area rate proceedings to which we are all committed. To subscribe to this position would be an abdication of the Commission's responsibilities under the Natural Gas Act to protect consumers against excessive rates.

The Commission further finds:

(1) Transco is a "natural-gas company" within the meaning of the Natural Gas Act, and the facilities for delivery of natural gas under the temporary certificate and for which a permanent certificate is sought will be used to transport natural gas moving in interstate commerce for resale to ultimate consumers. The construction and operation of such facilities together with the sale of gas by Transco, are subject to the requirements of subsections (c) and (e) of Section 7 of the Natural Gas Act.

(2) Transco is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Natural Gas Act and the requirements, rules and regulations of the Commission thereunder.

(3) The construction and operation of the above mentioned facilities, including the sale of natural gas to be purchased, are required by the public convenience and necessity, and a certificate therefor should be issued upon the terms and conditions of the order herein, which terms and conditions are required by the public convenience and necessity.

(4) South Texas is a "natural-gas company", and an "interstate pipeline" within the meaning of the Natural Gas Act and the Commission's regulations thereunder and its facilities, for which a certificate of public convenience and necessity is requested, will be used to transport natural gas moving in interstate commerce for resale to ultimate consumers. The construction and operation of such facili-

ties, together with the sale of gas by South Texas, are subject to the requirements of subsections (c) and (e) of Section 7 of the Natural Gas Act.

(5) South Texas is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Natural Gas Act and the requirements, rules and regulations of the Commission thereunder.

(6) The construction and operation of the facilities referred to in finding (4), including the sale of natural gas to be purchased by South Texas, are required by the public convenience and necessity, and a certificate therefor should be issued upon the terms and conditions of this order, which terms and conditions are required by the public convenience and necessity.

(7) The public convenience and necessity requires that South Texas' price to Transco be reduced to reflect the reduction in purchased gas costs effected by this order.

(8) The following applicants

	Docket Nos.
Skelly Oil Company	G-18638
Glen A. Martin *et al.*	G-18639
Coastal States Producing Company	G-18645
W. R. Ransome, Trustee	G-18684
Tenneco Corporation	G-18765
George H. Coates, Operator, *et al.*	G-18938
Coastal States Gas Producing Company, Operator and Southern Coast Corporation	G-19016
Carrl Oil and Hawn Bros.	G-19146
H. L. Brown	G-19175
Continental Oil Company	C160-71
Slick Oil Corporation	C160-206
Sunray-Mid-Continent Oil Company	C160-428
Woods Exploration and Producing Company	C160-600
Mokeen Oil Company *et al.*	C160-789
Tex-Star Oil & Gas Corp. *et al.*	C161-43
Prado Oil and Gas Company	C161-77

	Docket Nos.
Prado Oil and Gas Company	CI61-79
Coastal States Gas Producing Company	CI61-123
George H. Coates *et al.*	CI61-178
W. E. Bakke *et al.*	CI61-258
Coastal States Gas Producing Company	CI61-471
Coastal States Gas Producing Company	CI61-472
George H. Coates *et al.*	CI61-510
Russell Maguire *et al.*	CI61-530
Coastal States Gas Producing Company	CI61-539
Coastal States Gas Producing Company	CI61-566
Morgan Minerals Corporation	CI61-648
Jake L. Hamon	CI61-930

are now, or will become upon the commencement of the sale of natural gas proposed in these proceedings, natural gas companies within the meaning of the Natural Gas Act as independent producers of natural gas, as that term is defined in Section 154.91(a) of the Commission's Regulations, engaged in the sale of natural gas in interstate commerce for resale for ultimate public consumption, and such sales, together with the construction and operation of any facilities subject to the jurisdiction of the Commission necessary therefor, are subject to the requirements of subsections (c) and (e) of Section 7 of the Natural Gas Act.

(9) The independent producers referred to in the above paragraph (8) are able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Natural Gas Act and the requirements, rules and regulations of the Commission thereunder.

(10) The sale of natural gas as proposed by the independent producers referred to in the above paragraph (8) together with the construction and operation of any facilities subject to the jurisdiction of the Commission necessary therefor are required by the public convenience and necessity and a certificate authorizing the same should issue to

each of them upon the terms and conditions of the order herein, which terms and conditions are required by the public convenience and necessity.

(11) The public convenience and necessity requires that the initial price charged by the independent producers referred to in (8) above be not greater than 15 cents per Mcf at 14.65 psia and that the take-or-pay requirement in their contracts be revised in accordance with our final order in Docket No. R-199, commenced by Notice of Proposed Rule Making dated May 22, 1961.

The Commission orders:

(A) A certificate of public convenience and necessity is hereby issued to Transco in Docket No. G-18920, authorizing the operation of the facilities referred to above, all as more fully described in the application in these proceedings, for the transportation and sale of natural gas in interstate commerce as set forth therein upon the terms and conditions of this order.

(B) The general terms and conditions set forth in paragraph (c)(4) of Section 157.20 of the Commission's Regulations under the Natural Gas Act shall attach to the certificates issued to Transco in paragraph (A) and to South Texas in paragraph (C) hereof.

(C) A certificate of public convenience and necessity is hereby issued to South Texas in Docket No. G-18907, authorizing the construction and operation of the facilities hereinbefore referred to, including the operation of certain facilities of the Joint Venture, all as more fully described in the applications, and amendments thereto in these proceedings, for the transportation and sale of natural gas in interstate commerce as set forth therein, upon the terms and conditions of this order.

(D) As a condition to the certificate hereby issued to it, South Texas, on the date of issuance of this order, shall

commence charging, and shall continue to charge until lawfully changed in accordance with the Natural Gas Act, a rate for the sale of gas to Transco that shall represent its present initial charge of 20 cents per Mcf at 14.65 psia, less the reduction in its average cost of purchased gas effected by this order. Such average cost of purchased gas shall be computed as of the date of issuance of this order by using the rates ordered herein for producers as provided in paragraph (G).

(E) As an additional condition to the certificate issued hereby to it, South Texas is specifically required to submit to the Commission within 60 days of the issuance of this order a Form 2 Report for the year 1961 as prescribed in Section 260.1 of the Commission's Regulations under the Natural Gas Act, and in lieu of a pipeline form of tariff, shall file special rate schedules for its sales to its customers in accordance with this opinion and order and Section 154.52 of our Regulations, subject specifically to the acceptance by the Commission of the revised initial rate for the sale to Transco. In filing such special rate schedules, South Texas is granted a waiver of the requirements of Section 154.33 of our Regulations and the second sentence of section 154.32.

(F) A certificate of public convenience and necessity is hereby issued to each of the applicants referred to in finding (8) for the sale of natural gas in interstate commerce for resale as proposed in their applications, together with the construction and operation of any facilities subject to the jurisdiction of the Commission necessary therefor, upon the terms and conditions of this order.

(G) The certificates issued to the producer applicants listed below are hereby conditioned to prohibit any total initial price, including all reimbursements and charges, greater than 15 cents per Mcf at 14.65 psia from the date of issuance of this order until such prices may be lawfully changed in the manner provided by the Natural Gas Act:

Skelly Oil Co., Docket No. G-18638; Glen Martin, Docket No. G-18639; George H. Coates, Docket Nos. G-18938 and CI61-178; Continental Oil Co., Docket No. CI60-71; Sunray Midcontinent Oil Co., Docket No. CI60-428; Prado Oil & Gas Co., Docket Nos. CI61-77 and CI61-79; Coastal States Gas Producing Co., Docket Nos. CI61-471 and CI61-472; Russell Maguire, Docket No. CI61-530; Jake L. Hamon, Docket Nos. CI61-930; Mokeen Oil Company, Docket No. CI60-789; Tenneco Corporation, Docket No. G-18765; and Morgan Minerals Corp., Docket No. CI61-648.

(H) The certificates of all of the producer applicants referred to in (8) above shall be conditioned so that the take-or-pay requirement in each contract is subject to the provisions of our final order in Docket No. R-199 as of the effective date of that order.

(I) The certificates issued herein are not transferable and shall be effective only so long as each of said applicants continues the acts and operations herein authorized in accordance with the provisions of the Natural Gas Act and the applicable rules, regulations and orders of the Commission.

(J) The grant of the certificates herein shall not be construed as a waiver of the requirements of Section 4 of the Natural Gas Act or of Part 154 of the Commission's Regulations under said Act requiring the filing of rate schedules for the service herein authorized and is without prejudice to any findings or orders which may have been or hereafter may be made by the Commission in any proceeding now pending or hereinafter instituted by or against the applicants. Further, the action taken in these proceedings shall not foreclose nor prejudice any further proceeding or objection relating to the operation of any price or related provisions in the gas contracts here involved.

(K) All exceptions not granted herein are hereby denied.

(L) The examiner's decision, to the extent not inconsistent herewith, is hereby adopted as part of this opinion and order.

By the Commission.

Commissioner Ross concurring in part and dissenting in part for the reasons set forth in his separate opinion appended hereto.

Commissioner Morgan concurs in Commissioner Ross' concurrence and dissent, and will file a separate dissenting opinion at a later date.

J. H. GUTRIDE
Joseph H. Gutride
Secretary

Skelly Oil Company, *et al.* Docket Nos. G-18638, *et al.*

(Issued August 30, 1962)

Ross, Commissioner, *concurring* in part and *dissenting* in part:

I concur with the decision above in all respects except for that portion of the decision which severs the dockets of the four producers which received temporary certificates following the release of the September 28, 1960 Area Price Statement.

The refusal by the majority to decide these four dockets raises very pointedly the application by this Commission of the CATCO doctrine,[1] particularly during the interim period before conclusive area rates can be established. This refusal by the majority should also be read in the context of the Phillips decision by the District of Columbia Court of Appeals[2] because it is a concrete example of the problem discussed by that court although not necessary to the decision therein.

Basically, the issues as thus raised are first, are there any standards that the Commission must consider in determining interim guide line prices and secondly, is the validity of an interim guide line price subject to attack by intervenors in a hearing on a permanent certificate.

As to the first issue, it would seem that the majority stands for the proposition that the Commission in the interim period can by decree establish prices for temporary certification on the basis of its expertise without the necessity of paying any attention to in line prices in effect up to the moment of the decree, and most importantly, without the advice, consent, or representation of any interested

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[1] *Atlantic Refining Co.* v. *FPC*, 369 U.S. 378.

[2] *State of Wisconsin, et al.* v. *FPC*, Nos. 16175, *et al.*, November 30, 1961, CADC.

party. This is surely government by fiat and I, for one, view with alarm the asserted power inherent in an administrative body in price fixing of this nature.

In this case, the guide line rate is under attack. As a matter of fact, up to September 28, 1960, the majority concedes the validity of the attack. But, as to the period from September 28, 1960 to the present date, the majority here takes the position the avenues of attack are closed. In order to meet the objections of the attacking parties, it says we will lower our guide line rates in the future and will hold a hearing to determine whether the prices contained in temporary certificates granted between September 28, 1960 and the present are out of line. First of all, does this approach approximate the language of the now-famous CATCO case? I think not. Strange as it may seem, the majority says that on September 28, 1960 the in line price became something different because the policy statement says so. This hardly concurs with the philosophy of the CATCO case. In that case the Commission was reprimanded for granting a permanent certificate without paying due attention to in lineness. The Supreme Court recognized the dangers inherent to the consumers in allowing artificial jumps of this nature.

Also, it must be fully recognized that neither the producer nor the consumer is represented at the time these interim prices are established. It is government by decree, a summary and arbitrary action. Therefore, it becomes imperative to restrict the impact of such administrative decrees to truly cases of emergency and to curtail, as much as possible, the period of time such prices are to be in effect.

This brings us to the second and paramount issue: that is, whether the parties have a right to have a decision rendered on the evidence adduced on an application for a permanent certificate, particularly where the producer has already secured a temporary certificate based upon an

artificially high guide line price. A coroilary to this, is whether temporary guide line prices can be attacked in any way within a reasonable period of time by either the producer or the consumer.

Within the last few months, there has been considerable judicial expression concerning the importance of limiting the dangers inherent in this interim period and of granting all parties the due process normally afforded contested parties. For example, in *Wisconsin* v. *F.P.C.*, *supra*, Judge Prettyman and the majority of the court expressed the opinion that the Commission can adopt such interim prices and method of regulation. However, in that case, the majority stated emphatically that it was not considering whether a particular rate fell within the area of reasonable computation. It also stated,

> "Of course, the agency would be required to be alert for artificial impulses in such a fair area price and the avenues of attack by consumers would have to be kept open without obstruction." (Slip Opinion, Page 18)

The Supreme Court has also enunciated the necessity that the Commission render prompt decisions based upon the evidence at hand and the dangers in relying upon Section 5(a) proceedings in protecting the consumer. It should be remembered that the Commission in the CATCO case urged the proposition that it didn't make too much difference as to the level of prices in granting a certificate so long as the Commission could institute a Section 5(a) proceeding. The Commission claimed the consumer would adequately be protected. The Supreme Court was emphatic in stating that the overriding intent of Congress was to give the consumer full protective coverage as to the price. In the words of the Court, "The Act was so framed to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges" and the Commission is obliged to effectively carry out this

intent. Because Section 5(a) proceedings are prospective only, gas purchasers therefore, have no protection from excessive charges collected during the pendency of a Section 5 proceeding. See also Judge Fahy's dissent in *Wisconsin* v. *F.P.C., supra.*

With these cases in mind and the principles established therein, let us examine this situation more closely. Here, to repeat, we have a questionable interim guide line price established as has been demonstrated, by no or inaccurate concepts of in lineness. For two years a number of temporary certificates and one permanent certificate were issued based on this suspect price. Intervenors in this particular case sought to contest the validity of the price in these four dockets. Now they are being told, we admit you are right *but*, because we have granted temporaries to other producers before we realized the error, we are not going to discriminate and determine the price in these four contested dockets as excessive but rather compound the felony and allow everyone to collect the price. Surely, to do justice to the concept of interim prices, particularly when such prices are set without hearing and which are found to be excessive at the time of the establishment thereof and which are under attack in a fiercely contested hearing at such time, a fact known to the parties (see Hassie Hunt Trust, et al., Docket Nos. G-19115, et al, order of December 28, 1961), the Commission should not allow these prices to remain in effect any longer than necessary. This certainly is not keeping the avenues of attack open in line with Judge Prettyman's warning. It is only partial gratification to the consumer to realize that the prices paid for all gas dedicated during these two years in these districts may be lowered prospectively in a Section 5(a) type of proceeding. The least that could be done is to set the price as to these four producers at their proper level *now*.

The interim price situation is rapidly becoming a one-way street for the consumer. Judge Brown, in his recent

decision[3] claims that the Commission is using temporary certificates as the foundation for maintaining prices during the interim. The Court held that it was unlawful to condition the temporaries against price increases during the interim since it essentially violated the intent of the Natural Gas Act. In brief, it was unfair to the producer. As a matter of fact, I concur with his opinion. But I also feel it is unfair to ask the consumer to swallow temporary prices which may have been too high, as this case proves, and then to force them to rely upon the Commission's willingness to act sua sponte for relief. I am cognizant of the Commission's brief in its request for a rehearing in the *Hunt* case.[4] In my opinion, the position therein stated, namely, "the duration of these conditions will not, as the Court seemed to think, be measured by the length of time necessary to determine just and reasonable rates for natural gas in area rate proceedings (the "four to fourteen years" estimate of Judge Prettyman) but rather by the length of time necessary for the convening of an individual hearing on application for permanent certificate and for decision thereon," is entirely inconsistent with the majority here. These cases are applications for permanent certificates but where is the decision? Furthermore, the above-quoted statement is also inconsistent with the Commission's general practice of incorporating every application for a certificate in excess of the interim area price into the general area rate proceeding.

In my view, the administrative embarrassment of a backlog and the administrative difficulties of conducting individual hearings and making decisions therein does not warrant prohibiting either the producer from seeking legitimate increases or the consumer from contesting the validity of the interim prices if such interim prices are to be

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[3] *H. L. Hunt, et al.* v. *FPC*, Nos. 19065, *et al.*, July 19, 1962 CA 10.

[4] Ibid.

the way of life for a number of years. It is hardly any consolation to either party to say "don't worry, we will review them periodically and use our ouija board to set new prices." I am less than enthusiastic about my expertise to conjure up a fair price without the benefit of hearings in which parties can introduce evidence of in lineness, favored nation and triggering clauses in accordance with CATCO. Also, as Judge Fahy suggests in *Wisconsin* v. *F.P.C., supra*, in his dissent, the Commission should not be affirmed in failing to decide present cases. It is true that that case involved Section 4(e) and 5(a) proceedings but the philosophy is the same.

It seems to me after some experience on the Commission, that we would well consider the possibility of limiting temporary certificates to cases of real emergency and grant such certificates on the basis of our temporary ceilings if they have been measured by in lineness but emphasize that the price specified is to be conditioned to the price determined in the hearing on the permanent. We then should immediately set the case for hearing. At these hearings, parties, of course, could intervene and seek to show that the guide line prices are out of line, as in this case, or that there are triggering clauses. Following conclusion of these proceedings, all these permanent certificates should be consolidated in the Area Rate Proceeding as a Section 5(a) case in the event that such proceeding based on more adequate evidence in a contested case should disclose the interim guide line price as too high.[5] However, if a party

[5] At this point, it becomes imperative that the area rate proceeding in all areas be completed as soon as possible. The producer is protected by his right under Hunt to file and fight for an increase. The consumer on the other hand risks the possibility, if area rate proceedings are delayed and the initial guide line prices are set deliberately high to avoid indivdual charges of confiscation, that the ultimate area price has in fact already been set due to the great number of certificates based on the guide line prices which a Commission would be reluctant to change for any reason.

desires to seek a rate increase, then a hearing should be scheduled and at this hearing cost of service should be permitted. This would also give the Commission and all parties a measuring rod to use in the area rate proceeding.

In conclusion, it is my firm opinion that the Commission should grant the four producers a permanent certificate at 15¢ per Mcf effective this date.

CHARLES R. ROSS, Commissioner

APPENDIX C

Docket Nos. G-18638, *et al.*

Opinion No. 362A

OPINION AND ORDER ON REHEARING
MODIFYING OPINION AND ORDER

(Issued December 18, 1962)

SWIDLER, Chairman:

Applications for rehearing were filed to our opinion and order issued August 30, 1962 in the above-entitled proceeding by both producers and parties representing the interests of consumers.[1] On October 26, 1962, we granted rehearing in order to afford further time for consideration of the issues raised. In accordance with Section 1.34(d) of our Rules, on November 20, 1962, South Texas Natural Gas Gathering Company filed a response to the joint petition for rehearing of Long Island Lighting Company and The United Gas Improvement Company (UGI). While a number of the important issues are argued in the applications for rehearing, it would be repetitious to discuss again those that have been covered by the opinion. These include particularly some of the considerations in fixing the price line, the kind of evidence to be used in determining whether an initial price is in the public convenience and necessity, and the matter of refunds.

Several of the producers argue that in judging whether their proposed initial prices are "in line", we erred in making this determination as of the date of their contracts rather than the date of initial delivery. In the case of these producers the contracts were made before the issuance of

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[1] Texaco Inc., Prado Oil and Gas Company, Continental Oil Company, Sunray DX Oil Company, Jake L. Hamon, Morgan Minerals Corporation, Mokeen Oil Company, Tenneco Corporation, New York Public Service Commission and Long Island Lighting Company, and The United Gas Improvement Co.

our Statement of General Policy No. 61-1 on September 28, 1960, 24 FPC 818, but deliveries did not commence until afterwards. We used the date of contract because we are of the opinion that the execution of the contract is the significant act on the part of buyer and seller in determining the price.[2] The existence of high-priced contracts would have a general price raising effect even before deliveries were commenced. While, of course, we have no jurisdiction over a contract that never materializes in an interstate sale, it is a matter of discretion in the exercise of our regulatory function to require that the gas sold be sold under contracts that were in line as of the time they were executed. This concept is supported by *United Gas Co.* v. *Mobile Gas Corp.*, 350 U.S. 332 where the Court recognizes that "rates are established initially by the natural gas companies by contract or otherwise." To conclude, the present or future public convenience and necessity requires that, under the circumstances here, the contract prices must be in line as of the time the contracts were executed.

Furthermore, it is often impracticable to compare dates of delivery because the date of delivery is ordinarily not known to us until after a certificate is issued, unless deliveries have commenced under a temporary authorization. In the absence of such an authorization, we ordinarily grant permission to commence deliveries when it is convenient to the buyer and seller. This is to allow time for any construction that may be required before deliveries can commence. Therefore, a comparison of the in-line price on the date of delivery with the in-line price on the dates of deliveries under other contracts frequently cannot be made.

In connection with Jake L. Hamon contends that his contract in Docket No. C161-939, while dated September 25, 1960, before the Policy Statement, was really executed

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[2] *Continental Oil Co., et al.*, 27 FPC 96, 100; see also *The Ohio Oil Co.*, ... FPC ..., Docket No. G-15385, March 21, 1962.

December 1, 1960, the same date as two letter amendments. While the course of regulation should not depend on such technicalities as the parol evidence rule, Hamon has done nothing, beyond an assertion in his application for rehearing, to show the alleged date of execution. The application for a certificate, filed December 19, 1960, repeats the September 25, 1960 date of contract; a paragraph in the contract permits termination if a certificate is not issued by December 31, 1960, an entirely unreasonable provision for a contract executed December 1, 1960, because of notice requirements.

Several producers also argue that we erred in putting a condition in the certificates issued to the producers to the effect that the take-or-pay requirement in each contract is subject to the provisions of our final order in the rule-making proceeding in Docket No. R-199. In order to avoid any indefiniteness, as suggested by the producers, we shall provide as we did in *Panhandle Eastern Pipe Line Company*, — FPC — Opinion No. 350, Docket Nos. CP60-103, *et al.*, January 15, 1962, that while we shall condition our allowance of the proposed take-or-pay conditions in the instant proceeding so as to make them subject to our determination in the rule making proceeding,[3] in no event shall we require these producers to accept provisions for less than 80 percent of the annual contract quantities.

Prado Oil and Gas Company argues that assuming that its 16.0 cent initial contract price was not "in line", the price is justified by various special considerations. As our opinion notes,[4] while under the case law the in-line price will normally be the price at which certificates should be issued in the public interest and necessity pending ultimate

[3] For this purpose we believe it is immaterial that the rule making proposal in its present form would be applicable only to contracts made in 1961 and later.

[4] Opinion No. 362, mimeo. p. 13.

determination of the just and reasonable price, there may be special considerations where the just and reasonable price will be higher or lower than the in-line price. Prado says that it has built a gathering system and compressor station to facilitate its deliveries to El Paso. However, the record shows that most of the deliveries by others at 14.5, 14.6, and 14.8 cents are field rather than wellhead sales. Furthermore, Prado's testimony shows that 85 percent of its gas comes from but thirteen gas wells, while it is the small remainder that is produced from 192 oil wells. Thus the record indicates that any extensive gathering system applies to only a small portion of the gas that is recovered in connection with oil. The compressor facilities necessary to make the casinghead gas deliverable under the contract would be the responsibility of the seller to bring the gas up to pipeline quality. Furthermore, Prado's delivery pressure requirements for gas well gas are not as stringent as the majority of other contracts in the 14.5 to 15 cent price range.[5]

In addition Prado points to the fact that its contracts contain no indefinite pricing clauses, but it may be observed that almost all of the contracts below 15 cents contain only periodic escalations. Prado also states that the gas delivered by it contains approximately 1035 Btu's per cubic foot, while its contracts provide for a minimum of only 975 Btu's per cubic foot, so that, Prado argues, the ultimate consumers will receive an increase in heating value free of charge. It is true Prado's contracts do not contain a provision for an upward price adjustment for Btu content.

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[5] Prado is permitted to deliver gas as low as 250 lbs. psia when as many as four or one third of its gas wells are unable to deliver gas against line pressure.

but neither do other contracts below the 15-cent level[6] which were listed in the staff's basic exhibit as to comparative prices (Exhibit 24). Furthermore, we may note that Prado's contracts do not provide for a downward adjustment until the content falls below 975 Btu's per cubic foot while almost all other contracts for the years 1958 through 1960 in Texas Railroad District No. 4 provide for a downward adjustment when the Btu content falls below 1000 Btu's per cubic foot. Therefore, we are of the opinion that Prado has not shown that it should be permitted an individual addition to its price in excess of the "line" found in our opinion.

Continental Oil Company objects to our taking notice of certificates for sales in District 4 at prices ranging down to six cents per Mcf without opportunity to show the contrary. Our notice here of our prior orders was not a part of the decisional process in determining the line but merely part of our explanation of the scope of the staff exhibit, which treated sales at prices of 14 cents and above. Therefore further evidence on this matter would not affect the basis of our decision.[7]

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[6] The contracts are filed as rate schedules and were involved in the following certificate dockets: *Sunray Mid-Continent Oil Co.*, Docket No. G-19511, now Sunray DX Oil Co., Rate Sch. No. 185; *Renwar Oil Corp.*, Docket No. G-15518, formerly Rate Sch. No. 11, now Tenneco Oil Co., Rate Sch. No. 7; *Phillips Petroleum Co.*, Docket No. G-15809, Rate Sch. No. 322; *Cities Service Co.*, Docket No. G-16204, Rate Sch. No. 30; *W. L. Moody III*, Docket No. G-18758, Rate Sch. No. 1; *Seas Oil Corp.*, Docket No. G-19019, Rate Sch. No. 1; *Tennessee Gas Transmission Co.*, Docket No. G-19182, Rate Schedules F-55 and F-56. The rate schedules all contain specific provisions for dehydration while this is not required in Prado's rate schedules (Nos. 1 and 2).

[7] We have taken official notice of our own orders or reports filed with us in other proceedings. *Continental Oil Co.*, 15 FPC 641; *Wisconsin v. FPC*, 201 F.2d 183 (CADC), certiorari denied, 345 U.S. 934.

In its application for rehearing the New York Public Service Commission (PSC) criticizes the basis employed in establishing the price line contending that the price line should be 14.6 cents rather than 15 cents. In the first place PSC notes that we have not identified the temporary certificates at the 14.6 cent, 14.8 cent and 15.0 cent levels that have subsequently been made permanent in other proceedings. These are listed as under temporary certificate in Exhibit 24 and are set forth in Appendix A hereto.

PSC contends that as to the two contracts at 14.8 cents [8] which are listed as permanent in Opinion No. 362, the stated price is 14.613 cents per Mcf. It is true that the base price is 14.613 cents, but we used 14.8 cents so as to include the base price plus tax reimbursements in making comparisons. *United Gas Improvement Co.* v. *F.P.C.*, 283 F.2d 817 (CA 9) certiorari denied 365 U.S. 881.

PSC's principal contention with respect to our determination of the price line is that we were relying on the two sales at 14.8 cents (or 14.613 cents as PSC would have it) and one sale at 15.0 cents [9] and that it was not a party in these proceedings because the routine notice [10] did not alert it to the significance of the price. In our opinion the notice

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[8] The 14.8 cent prices were contained in contracts of *Renwar Oil Corp.*, Docket No. G-15518 and *Phillips Petroleum Co.*, Docket No. G-15809.

[9] *Sunray Mid-Continent Oil Co.*, Docket No. G-19511.

[10] Originally as PSC points out, the *Sunray* proceeding as Docket No. G-17051 at the 15-cent price had been consolidated with *Texas Illinois Natural Gas Pipeline Company, et al.*, Docket No. G-14829, from which PSC had been excluded and which was remanded in *PSC* v. *FPC*, 295 F.2d 140 (CADC). The notice in Docket No. G-19511 which was published in the Federal Register sets forth that Sunray had filed an application for a certificate and that it proposes to sell natural gas in interstate commerce to South Texas for resale under a gas sales contract dated July 1, 1959.

was sufficient to alert PSC, as in fact it had been alerted by a similar notice with respect to a filing where it did intervene.[11]

In any event, PSC takes a too narrow view of our determination of a price line. In determining the line we were not relying merely on three contracts. We saw that there were a number of contracts involving substantial volumes of gas from 14 to 18 cents under permanent certificate. We saw that most of those above 15 cents were subject to litigation while most of those below 15 cents were not subject to litigation. We also gave a more limited degree of consideration to the pattern of untainted sales prior to 1958 and to the price range of contracts made during 1958-1960, resulting in temporary certificates including in particular those subsequently made permanent at that price. Fifteen cents, in our judgment, represented a reasonable limit on prices arrived at in contracts dated during 1958, 1959, and 1960, not subject to litigation.

PSC objects to our deferring action on the applications of four producers whose contracts were dated after September 28, 1960, when our Policy Statement was issued. As explained in our opinion we are deferring action so that all parties will have opportunity to show the effect of the 15-cent price established here, the 16-cent ceiling adopted for future contracts or the 18-cent price established on September 28, 1960. This is not a final order with respect to these producers, and our action at this time is an appropriate procedural step in view of the absence of evidence on the effect, if any, of the Commission's adoption of the September 28, 1960 ceiling prices on the pricing picture.

PSC finally argues along with Long Island Lighting Company and The United Gas Improvement Company that we

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[11] See the notice in the first *CATCO* case, *Continental Oil Co.*, 17 FPC 574, 732, 880; 21 F.R. 7783.

should have required refunds by the producers as a result of our determination of the 15-cent in-line price. The essence of our conclusion on this point is that it would be inequitable to require the producers to make refunds where they were issued temporary certificates in general language without specific provision for refunds.[12] They undertook service thereby binding themselves to deliver gas until relieved by us under a certificate that did not require nor suggest a refund. The situation was different in the *CATCO* case.[13] There was no temporary certificate and the permanent certificate was the subject of a timely petition for review. Moreover, service there had not begun until

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[12] Typical language in the temporary certificates provides in part:

> "This acceptance for filing shall not be construed as constituting approval of any rate, charge, classification, or any rule, regulation or practice affecting such rate or service contained in the rate filing; nor shall such acceptance be deemed as recognition of any claimed contractual right or obligation associated therewith; and such acceptance is without prejudice to any findings or orders which may be made in the final disposition of this proceeding or any other findings or orders which have been or may hereafter be made by the Commission in any proceeding now pending or hereafter instituted by or against your company."
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> "This constitutes all requisite temporary authorization to commence the sale of gas, but such authorization and acceptance of the rate schedule are without prejudice to such final disposition of the certificate application as the record may require and, furthermore, once service is commenced under this authorization it may not be discontinued without permission of the Commission issued pursuant to the provisions of the Natural Gas Act."

[13] *Continental Oil Company, et al.*, 27 FPC 96.

after judicial proceedings had been initiated,[14] so that the rates were challenged before any revenues were collected.

A refund has been required when the permanently certificated rate is less than the temporary one, but in such a case specific language advising the parties of the risk they took if they accepted the temporary certificate has uniformly been used. Since in the present proceeding there is no such provision in the temporary certificates, to proceed now and order the producers to make refunds would not be equitable regardless of any ultimate right we may have to order such refunds.

The Long Island Lighting Company and The United Gas Improvement Company contend that the costs of South Texas may be reduced as a result of a decision on the four sales severed from these proceedings as well as other sales involved in the *Amerada* proceedings[15] and as a result of decisions on the effects of a consolidated federal income tax return and liberalized depreciation tax accounting.[16] Therefore, they argue that the certificate issued to South Texas should be conditioned to require a further reduction and refunds as contemplated by the examiner. We agree that this suggestion of the interveners in part has merit. We shall therefore require that South Texas file rate changes to reflect any change in purchased gas cost effected by the *Amerada* proceeding. However, we shall not require South Texas to make refunds, for in accordance with our Opinion No. 362 herein the producers would not be required to make refunds. This condition would not work an injury on South Texas because it would not affect the return, but

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[14] The final order challenged was issued June 24, 1957 (17 FPC 880), the petition for review was filed October 7, 1957, but deliveries didn't commence until July of 1958.

[15] *Amerada Oil Company, et al.*, Docket Nos. C162-1544, *et al.*

[16] Specifically, *Cities Service Gas Co.*, Docket No. G-18799, and *Alabama-Tennessee Natural Gas Co.*, Docket No. G-5471, *et al.*

would merely pass along savings on producer sales made to it. However, the later determination of the federal income tax question would appear to create an indefinite condition that would be inequitable to South Texas. In view of the fact that the tax question is comparatively minor in effect, we will not condition South Texas' certificate to give effect to decisions in other cases which may not be decided with finality for some time. Furthermore, it would not be in the public interest to leave the present proceeding open pending the decision of these questions which are of no great moment here.

Long Island Lighting and UGI make the further point that reduction in the producer rates may lead to a higher rate of return for South Texas than its contemplated 7.34 percent. In the first place, as pointed out by South Texas, the 7.34 percent return will not be earned by it under its proposed rates. Further, it is entirely speculative as to what return will be earned under a different price structure. In any case this is not a rate case. We do not think that the earnings contemplated by South Texas are so disproportionate as to be inconsistent with the public convenience and necessity.

In its response South Texas objects to Long Island Lighting and UGI requesting the examiner's refund condition which is dependent upon a cost filing to be made by South Texas. South Texas says that it has made this cost filing and no further cost filing should be required. The cost filing made by South Texas on February 1, 1962, was apparently made in response to our prior order of November 22, 1960, in *Texaco Inc.*, 24 FPC 979, on which we granted rehearing. We have utilized this cost filing in determining whether to grant a certificate to South Texas and whether to condition that certificate. No further cost filing, if that was intended by Long Island Lighting and UGI is necessary, and the filing of February 1, 1962, will be admitted into evidence.

It has been brought to our attention that by amendment filed July 30, 1962, to the application in Docket No. CI60-206 Midhurst Oil Corporation has become the successor to Slick Oil Corporation. We shall accordingly provide that Midhurst be substituted for Slick in our Opinion and Order No. 362.

The Commission further finds:

(1) The assignments of error and grounds for rehearing set forth in the applications for rehearing filed herein present no facts or principles of law which were not considered by the Commission when it issued its Opinion No. 362, or which having now been considered warrant any change or modification of such opinion except as specified below.

(2) The request of Jake L. Hamon in Docket No. CI61-930 for severance should be denied.

The Commission Orders:

(A) The applications for rehearing filed in the above-entitled proceedings by the applicants for rehearing listed in footnote 1 above are hereby denied except as specified below.

(B) The request of Jake L. Hamon for severance of Docket No. CI61-930 is hereby denied.

(C) The following provision shall be added to paragraph (H) of our previous order. "Upon the issuance of such final order the producers accepting the certificates herein issued shall file within 30 days amended rate schedules in conformity therewith, acceptable to the Commission; provided, however, that the producers shall not be required to file take-or-pay provisions for less than 80 percent of the annual contract quantities."

(D) Paragraph (D) of our order is hereby amended to require that South Texas within 60 days after issuance of our final orders in *Amerada Petroleum Corporation, et al.*, Docket No. CI62-1544, shall file a rate for service to Transco that shall reflect any decrease in purchased gas costs effected by Docket No. CI62-1544; such change shall be effective coincidentally with the effective date of the *Amerada* rate change. At the time of making such rate filing South Texas shall also file a computation showing the derivation of such rate changes, which shall be computed as of the date of issuance of the final order in Docket No. CI62-1544 using the rates ordered therein. Such rate filing shall be subject to approval by the Commission.

(E) The cost filings made by South Texas on February 1, 1962, and by the Joint Venture on February 12, 1962, are hereby admitted into evidence.

(F) Midhurst Oil Corporation is hereby substituted for Slick Oil Corporation in Docket No. CI60-206.

By the Commission. Commissioner Ross dissenting in part to the extend that this order is inconsistent with his dissenting opinion. Commissioner Morgan not participating.

(Signed) J. H. Gutride
Joseph H. Gutride,
Secretary.

APPENDIX A

Company	Docket No.	Date of Order Granting Permanent Certificate	Rate Schedule	Price*	Est. First Month Volume (Mcf)
Texaco, Inc.	CI60-70	6-27-61	212	14.6	26,350
Little Giant Oil Co. of Texas	CI61-319	6-27-61	1	14.6	60,000
Blanco Oil Co.	CI61-82	1- 8-62	7	14.8	40,000
Graridge Corp.	CI61-519	8- 7-61	6	15.0	60,000
Cities Service Co.	CI61-1131	12-27-61	36	15.0	61,710

*In each case the price is the initial price plus tax and other reimbursements as shown in Exhibit 24.